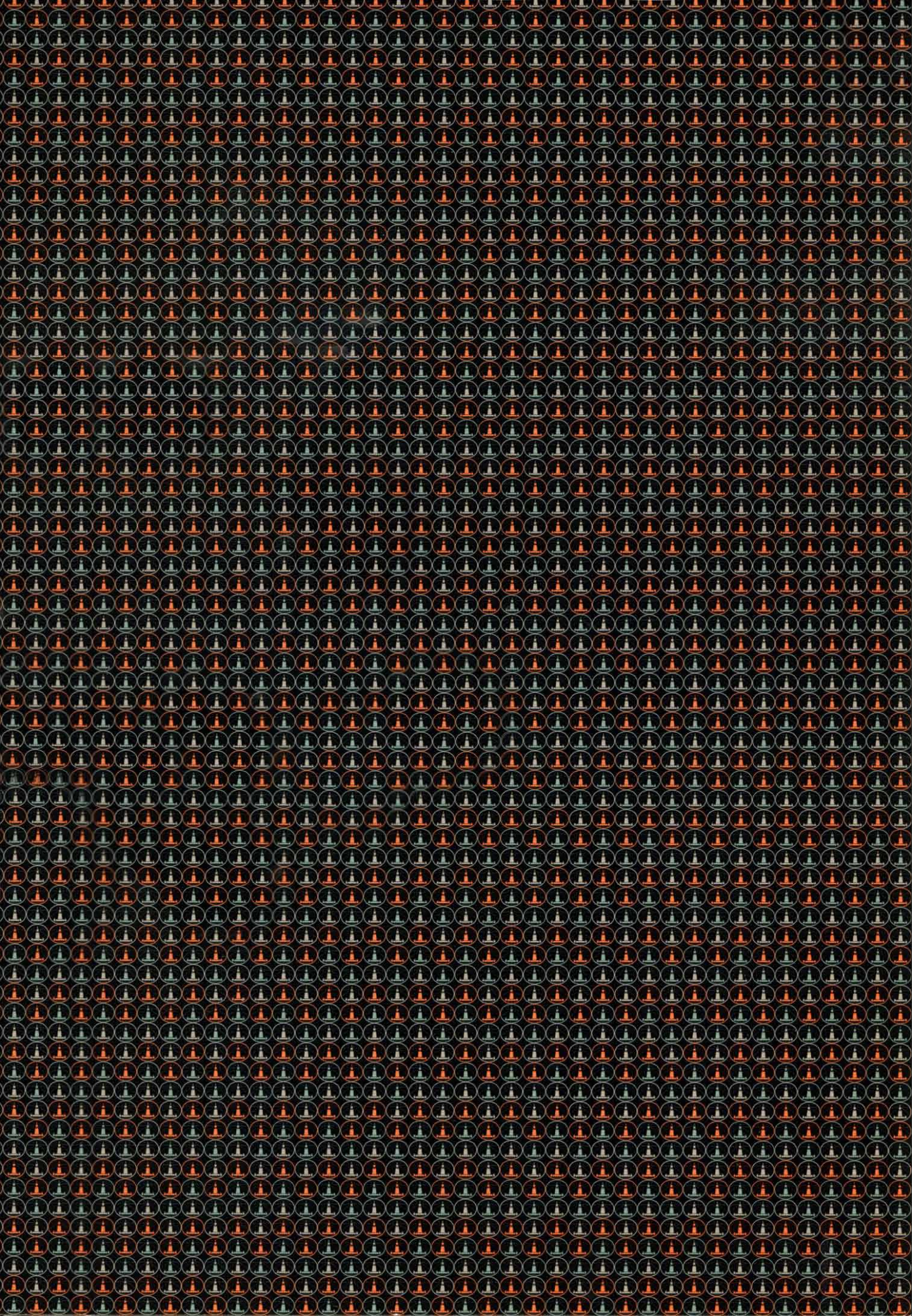
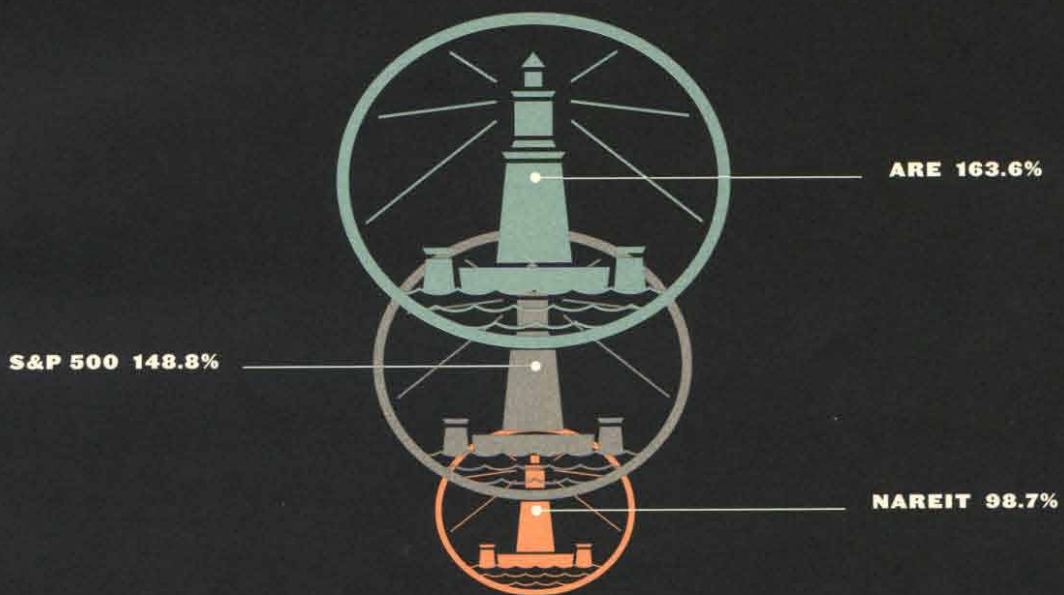




Under good market conditions, as well as during volatile times, Alexandria's strategy is solid, providing shareholders with a steady and consistent growth opportunity. Growing a quality asset base and servicing our tenants is foremost on our minds. By providing state-of-the-art facilities that meet the demanding needs of the scientific research community, ARE is becoming the landlord of choice for the life science industry in its target markets, attracting tenants that are the leaders in their business segments.



“Our niche focus made us less susceptible to swings impacting the broader REIT market.”

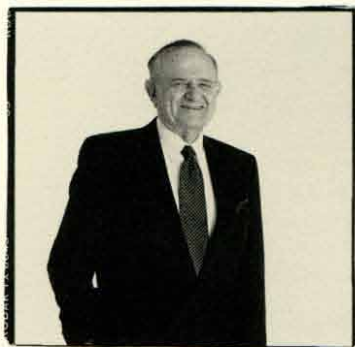


Alexandria Real Estate Equities, Inc.'s performance compared to NAREIT Index and S&P 500 Index (Total return performance May 28, 1997 to December 31, 1998)

ALEXANDRIA IS THE ONLY PUBLICLY TRADED REAL ESTATE INVESTMENT TRUST (REIT) THAT FILLS A UNIQUE NICHE WITH A PRINCIPAL INVESTMENT FOCUS ON STRATEGICALLY LOCATED PROPERTIES CONTAINING OFFICE/LABORATORY SPACE. ALEXANDRIA ACQUIRES AND MANAGES FACILITIES, AS WELL AS EXPANDS AND CONVERTS SPACE TO MEET THE NEEDS OF LIFE SCIENCE INDUSTRY TENANTS. ALEXANDRIA WILL ALSO BUILD-TO-SUIT AND RETROFIT SPACE AS TENANTS REQUIRE. THE COMPANY'S STRATEGY IS TO BE THE LANDLORD OF CHOICE TO ORGANIZATIONS WHICH UTILIZE OFFICE/LABORATORY SPACE.

COVER PHOTO: 620 MEMORIAL DRIVE, CAMBRIDGE, MASSACHUSETTS

COVER QUOTE: JOEL S. MARCUS, CEO



JERRY M. SUDARSKY
CHAIRMAN
OF THE BOARD



JOEL S. MARCUS
CHIEF EXECUTIVE
OFFICER

Dear Shareholders

1998 was our first full year as a public company. During the year, we continued to successfully execute our niche operating strategy, with the objective of becoming the landlord of choice for the life science industry in our target markets. In fact, we now own and operate 17 properties in the suburban Washington D.C. region. We believe we are now the largest public real estate investment trust (REIT) owning office/laboratory space in that market, and believe that we have developed a very positive reputation among the laboratory user tenant base located there. We are proud to have achieved this goal so quickly.

The year was a volatile year for the stock market, and the REIT industry was particularly susceptible to adverse market conditions. Our niche focus, however, made us less susceptible to swings impacting the broader REIT market. Due to the stable demand and limited supply characteristics of laboratory space, our asset base was less sensitive to the traditional supply/demand cycles affecting office properties generally.

At the same time, the tightening of the financial markets resulted in a decrease in competition for quality acquisitions. This presented us with an opportunity to make better quality deals at higher yields. During the year, we increased our line of credit by \$100 million, at more favorable rates, which has provided us with additional financial flexibility to be opportunistic in our target markets.

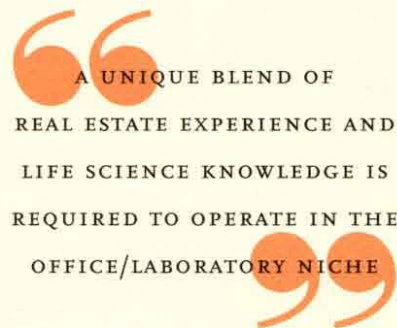
An important factor contributing to our steady growth is the broad and diverse industry segments in which our tenants operate. Scientific research expenditures by both the private and public sectors continued to grow. For example, during the last 12 consecutive years, there has been an increase in annual research and development spending by the pharmaceutical industry, growing from \$3.4 billion to over \$18 billion today, according to the Pharmaceutical Research and Manufacturers of America. Research and development spending by the pharmaceutical industry last year increased 11%. This is coupled with the National Institutes of Health (NIH) budget, which was increased over 14% to \$15.6 billion this fiscal year, and which is anticipated to double in five years. This year represented the largest annual increase in the NIH's budget. Spending increases reflect the aging of the U.S. population and suggest that the demand for office/laboratory space to accommodate the increase in scientific research should continue to be strong.

A unique blend of real estate experience and life science knowledge is required to operate in the office/laboratory niche. The skills of our management team enable us to be the focused leader within this niche. With more than 150 years of combined experience in both real estate and life science, our management team has the

expertise needed to successfully integrate these two disparate industries, providing positive results for our tenants and shareholders.

During the year, we named James H. Richardson as President. Jim joined us in August 1997 as Senior Vice President for Acquisitions. Jim's experience in real estate acquisitions and development, specializing in the life science sector, has served our company well. Jim has not only proven himself as an astute deal negotiator, but also a skilled strategist and manager.

During 1998, we enhanced our operational infrastructure to include regionally-based operations and have opened our third such operation in the suburban Washington, D.C. market. With a focus on building a strong franchise in each of our target markets, these operations allow us to be more responsive to tenants by maintaining an important presence in the community in which they live and work.



A UNIQUE BLEND OF
REAL ESTATE EXPERIENCE AND
LIFE SCIENCE KNOWLEDGE IS
REQUIRED TO OPERATE IN THE
OFFICE/LABORATORY NICHE

INTERNAL AND EXTERNAL STRATEGIC GROWTH MODELS

Since our founding, we have recognized the need for multiple business models and strategies to achieve our growth objectives. Our strategy has been to limit inherent risk by realizing consistently strong internal growth while adhering to a strict discipline with respect to acquisitions and external growth. Our three operating models: 1) acquire and manage 2) expand, retrofit and convert and 3) build-to-suit, have enabled us to generate growth through multiple sources while serving the important and complex facilities needs of the life science industry.

In our first full year as a publicly-traded company, we achieved significant growth both internally and externally, making positive progress utilizing each of our operating models. Since our initial public offering, the number of

buildings in our portfolio has more than tripled. During 1998, we completed approximately \$240 million in acquisitions, acquiring 29 properties, which added approximately 1.85 million square feet to our portfolio. Adhering to our targeted acquisition strategy and strict criteria, all of our 1998 acquisitions are located in one of the seven identified key target markets that we believe represent dominant hubs for scientific research in the United States. We are steadily progressing in our goal of building an important business franchise in each of these target markets.

We have consistently maintained a focus on maximizing our internal growth potential through contractual rental rate increases,

Hutchinson Cancer Research Center). When purchased approximately three years ago, a major consideration was to substantially re-lease the building. We successfully re-leased 89% of the 82,000 square feet that expired in 1998, raising rental rates on the expiring space from an average of \$24.77 per square foot to \$31.29 per square foot. We are currently in the process of leasing the remainder of the available space.

Conversions present us with another important growth opportunity. Due to the demanding facility needs of the life science industry, we have an important opportunity to convert existing office into laboratory space at generally higher rents.

“AN IMPORTANT FACTOR CONTRIBUTING TO OUR STEADY GROWTH IS THE BROAD AND DIVERSE INDUSTRY SEGMENTS IN WHICH OUR TENANTS OPERATE”

retenanting and releasing, effective cost control, and expansions and conversions. During the year, we reported same-store growth of 4.0% on a generally accepted accounting principles basis, representing strong internal growth that we believe will have a greater impact on our results as our portfolio increases in size. Occupancy rates for our operating properties at the end of the year were approximately 96%, with substantially all of the vacancies being in office/warehouse, rather than laboratory space. A substantial number of our existing leases are at rents below market, which should allow for positive growth in the future. In 1998, rent escalations were included in approximately 83% of our leases, with increases generally fixed between 2.5% to 4% annually.

Also in 1998, we completed our largest lease roll-overs to date in the Alexandria Seattle Life Sciences Center (formerly known as the Fred

During the year, we initiated our first two development projects, breaking ground on Alexandria Research Center at Torrey Pines (San Diego, California) and on Alexandria Research Center at Gaithersburg (Maryland). The Torrey Pines facility is comprised of two buildings, encompassing approximately 90,000 square feet, with leasing underway. Alexandria Research Center at Gaithersburg represents our largest development project to date, comprising four buildings and approximately 348,000 square feet. The first building in the complex, comprising 120,000 square feet, is being constructed on a build-to-suit basis. Occupancy is expected to commence by the end of 1999. The remainder of the land is for future build-to-suit opportunities. These projects significantly expand our presence in the San Diego and suburban Washington, D.C. markets and are representative of the development

opportunities that exist in our office/laboratory market niche.

Our growing tenant base includes many of the leaders in the life science industry segments. During the year we welcomed Pfizer Inc. to our life science tenant base. We are proud of this tenant base, which also includes Novartis AG, the U.S. Food and Drug Administration, Scripps Research Institute, MedImmune, Inc., Agouron Pharmaceuticals, Inc. (Warner Lambert), University of Washington, and the Gillette Company, to name just a few. We consider ourselves strategic partners with our tenants with respect to their scientific research work, contributing high quality office/laboratory space and facilities management that meet the unique needs of this broad and diverse industry.

FINANCIAL HIGHLIGHTS

Our financial performance was consistent with the goals we set for ourselves last year. Funds from Operations (FFO) for the year were approximately \$29.7 million on revenues of approximately \$61 million, exceeding consensus analysts' FFO per share estimates for each quarter. Importantly, during the second half of the year, we expanded our unsecured credit facility to up to \$250 million, while reducing the interest rate schedule. This has enabled us to achieve greater balance sheet flexibility during a tighter credit environment. We also strengthened our financial position during the year through a unit placement of 1,150,000 shares, netting us approximately \$32.7 million.

OUTLOOK FOR 1999

As we enter the last year of the 20th Century, we believe that our operational infrastructure is substantially in place to support our continued growth. We intend to continue to execute our multi-prong business strategy, maintaining a balance between internal and external growth, while managing balance sheet flexibility.

1999 will be an important year in managing the roll-over of leases in our portfolio. Forty-seven leases, representing approximately 10% of the square feet in our portfolio, will expire during the year. We are well into the releasing process on many of the expiring leases. Due to our extensive network and experience in the life science industry, we believe we have a heightened ability to locate attractive tenants and negotiate favorable lease terms. As many of the leases are currently at rental rates below market, we also view this as an opportunity to increase rental rates, with the potential of adding to our FFO growth during 1999.

We are proud to be prominently positioned within the REIT industry, enjoying broad analyst coverage and outperforming many of our peers. As we enter 1999, our mission remains the same: provide a unique growth opportunity for our shareholders and become the landlord of choice for the life science industry in each of our target markets.

In closing, we would like to thank our shareholders, tenants and employees for their continuing support and confidence in us.



JERRY M. SUDARSKY
CHAIRMAN OF THE BOARD



JOEL S. MARCUS
CHIEF EXECUTIVE OFFICER



STRATEGIC GROWTH OF PORTFOLIO

ARE's portfolio of properties has more than tripled in size since the IPO, reflecting the existing need for quality laboratory space. At the end of 1998, ARE had a total of 51 properties, comprising approximately 3.6 million square feet.



STRATEGY, EXECUTION AND FINANCIAL PERFORMANCE

ARE surpassed consensus analysts' FFO estimates every reporting quarter since its IPO, achieving FFO growth of approximately 35%, compared to last year. Same store growth of 6.5% on a cash basis is among the highest for REITs. Demonstrating prudent fiscal planning, ARE increased its credit line during the year at more favorable rates, enabling the company to maintain balance sheet flexibility.



ENHANCEMENT OF MANAGEMENT TEAM

An experienced management team in both the real estate and life science industries is the key to ARE's success. During the year, ARE enhanced its management team with the appointments of James H. Richardson to President and Vincent R. Ciruzzi to Vice President - Construction and Development. The expertise that management possesses uniquely qualifies ARE to be the landlord of choice for the life science industry.



ASSET AND TENANT SERVICES

Emphasizing its commitment to tenants, ARE is establishing regionally-based operations enabling the company to be more responsive to tenants' complex facilities needs. Working side-by-side with its tenants, ARE provides value-added services and capital to ensure quality facility management and state-of-the-art improvements, when required, to achieve maximum tenant satisfaction.



INTERNAL GROWTH

In addition to achieving consistent growth through rent escalations and lease roll-overs, the nature of ARE's tenant base provides the company with a unique growth model for converting standard office space into higher rent laboratory space. Lease roll-overs with respect to rental space which is currently below market, may provide for future FFO growth.



EXTERNAL GROWTH

During 1998, ARE completed approximately \$240 million in acquisitions, acquiring 29 properties, which added approximately 1.85 million square feet to its portfolio. During the year, ARE had the financial flexibility to be opportunistic in a real estate market that had seen a decrease in well capitalized buyers, resulting in better quality transactions at higher yields for the company. ARE's acquisition strategy has been focused on high quality facilities in seven key scientific research hubs with the goal of developing a strategic franchise in each such market.



INITIATED FIRST DEVELOPMENT PROJECTS (SAN DIEGO & GAITHERSBURG)

Initiating its first development project, ARE commenced construction in April on Alexandria Research Center at Torrey Pines in San Diego. Later in the year, construction of Alexandria Research Center at Gaithersburg, Maryland began. These projects expand ARE's presence in these two key hubs and represent the implementation of an important external business growth strategy.

Gene Logic

The Gaithersburg area improves our visibility and is well suited for recruiting and future growth. There is a tremendous shortage of space in Maryland and ARE moved expeditiously, quickly identifying a suitable building and financing significant improvements. ARE is a good resource for our building needs, whether it's obtaining contractors to perform maintenance on the building or providing benchmark information for operating costs. They also provide us enough flexibility to operate our dynamic business.

Michael J. Brennan
M.D., Ph.D.
Chief Executive Officer

Mark D. Gessler
President and Chief Operating Officer

708 QUINCE ORCHARD ROAD, GAITHERSBURG, MARYLAND

Located in the heart of the Gaithersburg research community, this 49,225 square foot, fully modernized facility was a retrofit project to meet Gene Logic's specific requirements. On the cutting edge of the genomics revolution, Gene Logic required state-of-the-art laboratory and office space to house their novel screening technologies and proprietary gene expression databases for identifying new drug leads.



MARK GESSLER

MICHAEL BRENNAN

BOOTH

MELVIN



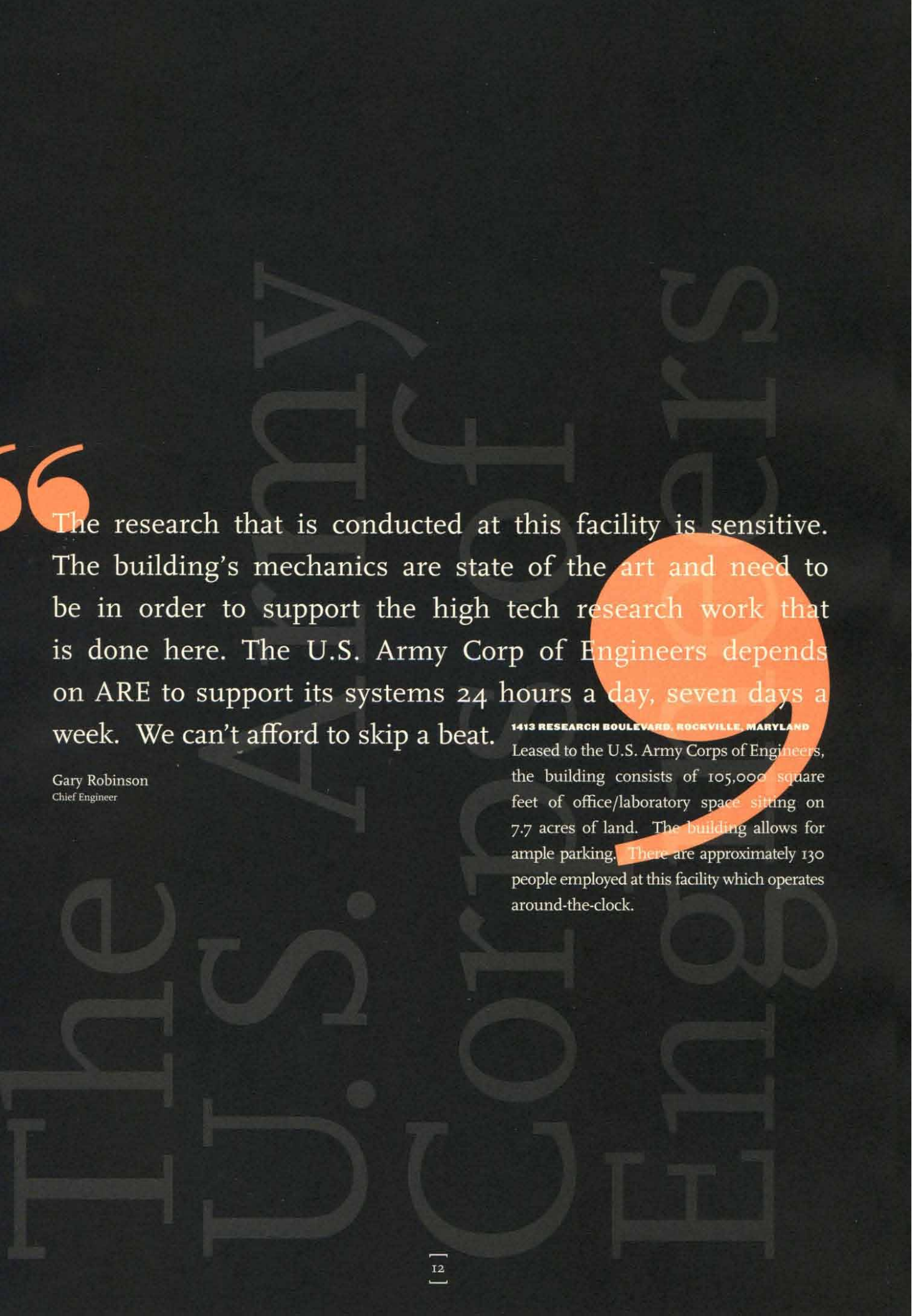
MedImmune, Inc.

ARE's knowledge of life science companies' space needs permits them to address requests expeditiously. They have been quite responsive in reviewing all proposed modifications and any other requests. They have worked with us on expansion projects, including a willingness to finance improvements. It is an added benefit that they have someone based locally, but even before then, we could always count on them to take care of whatever we asked of them.

25/35 WEST WATKINS MILL ROAD, GAITHERSBURG, MARYLAND

The facility has been designed specifically for MedImmune, a top-tier biotechnology company which markets three products and is developing other product candidates focused on infectious diseases and transplantation medicine. The facility consists of two one-story brick buildings comprising a total of 84,668 square feet which houses office and laboratory space as well as a GMP-designated manufacturing suite.

Melvin D. Booth
President and Chief Operating Officer



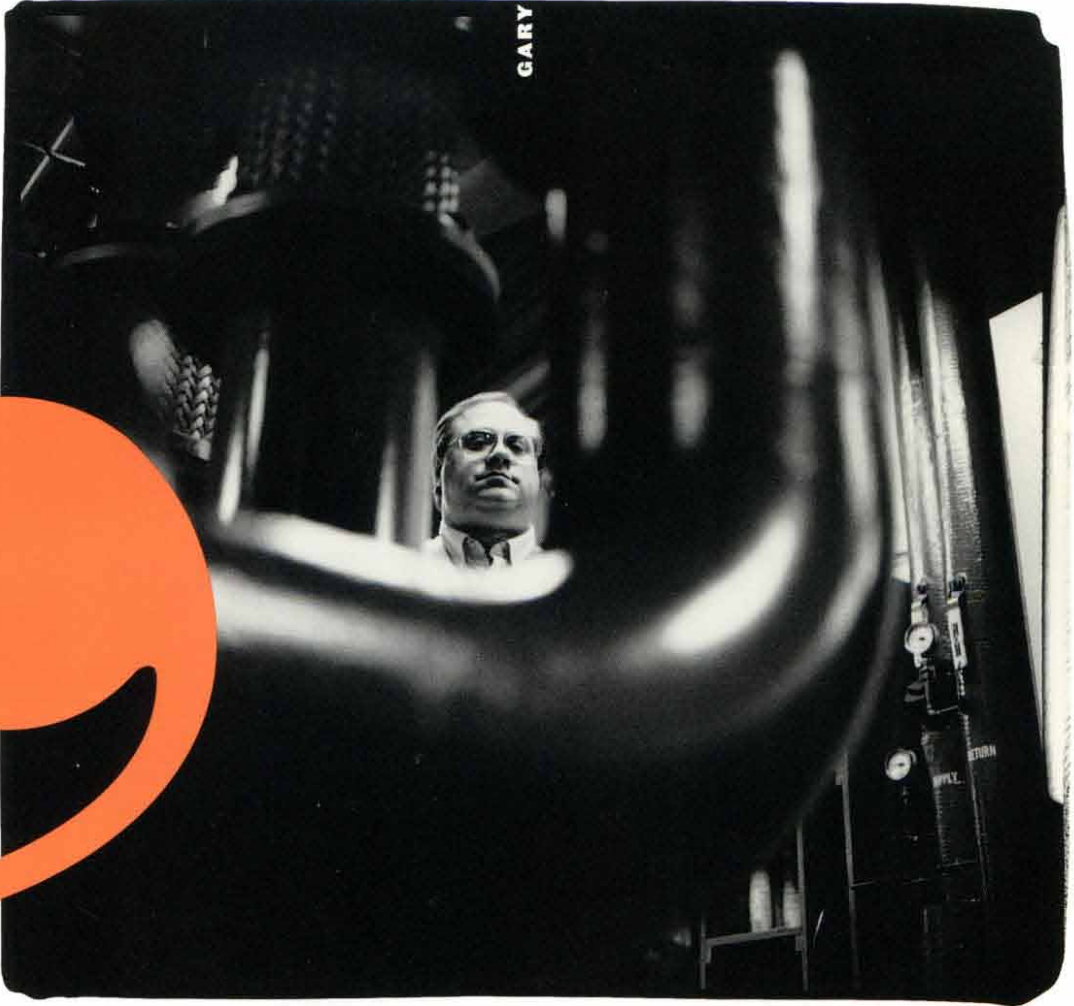
The research that is conducted at this facility is sensitive. The building's mechanics are state of the art and need to be in order to support the high tech research work that is done here. The U.S. Army Corp of Engineers depends on ARE to support its systems 24 hours a day, seven days a week. We can't afford to skip a beat.

Gary Robinson
Chief Engineer

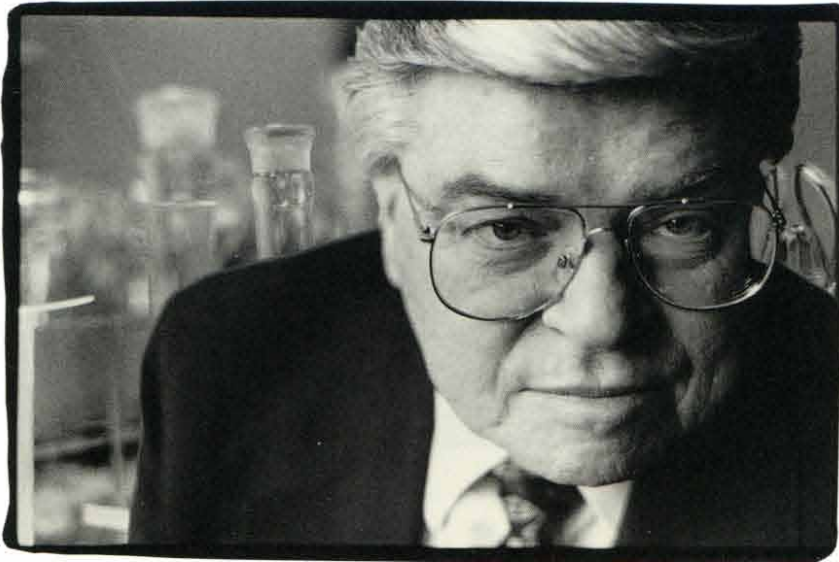
1413 RESEARCH BOULEVARD, ROCKVILLE, MARYLAND

Leased to the U.S. Army Corps of Engineers, the building consists of 105,000 square feet of office/laboratory space sitting on 7.7 acres of land. The building allows for ample parking. There are approximately 130 people employed at this facility which operates around-the-clock.

GARY ROBINSON



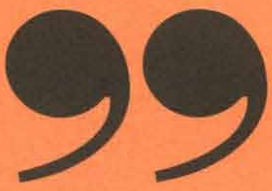
HENRY GIUGIATA



Gillette
Medical
Evaluation
Laboratories
Gillette



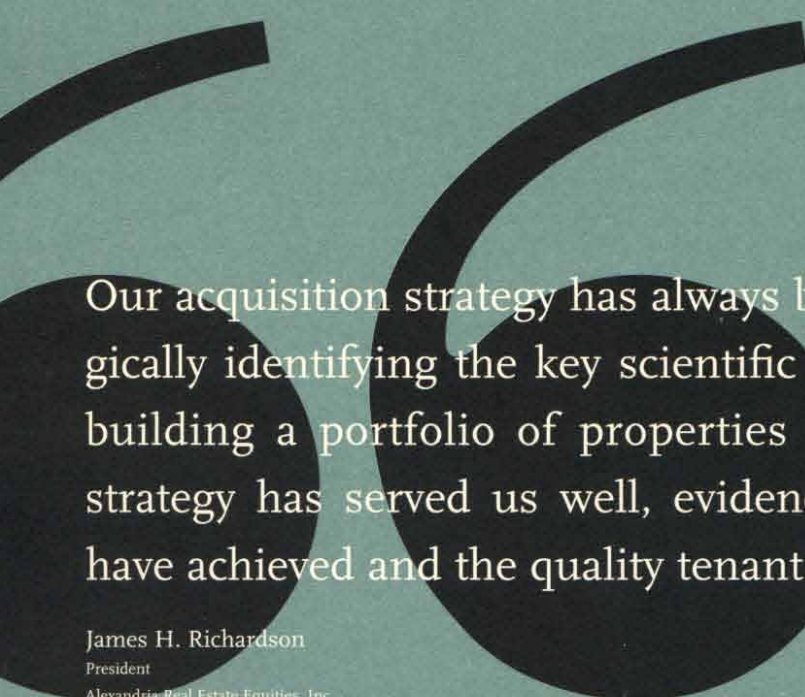
We managed our own retrofit and ARE was flexible, not at all rigid in allowing us a lot of independence to create the space to fit our own needs. ARE is easy to deal with and the build-out went smoothly. During the process, ARE was helpful in benchmarking references and provided us budgets in a timely manner.



Henry Ciuchta, Ph.D.
President

401 PROFESSIONAL DRIVE, GAITHERSBURG, MARYLAND

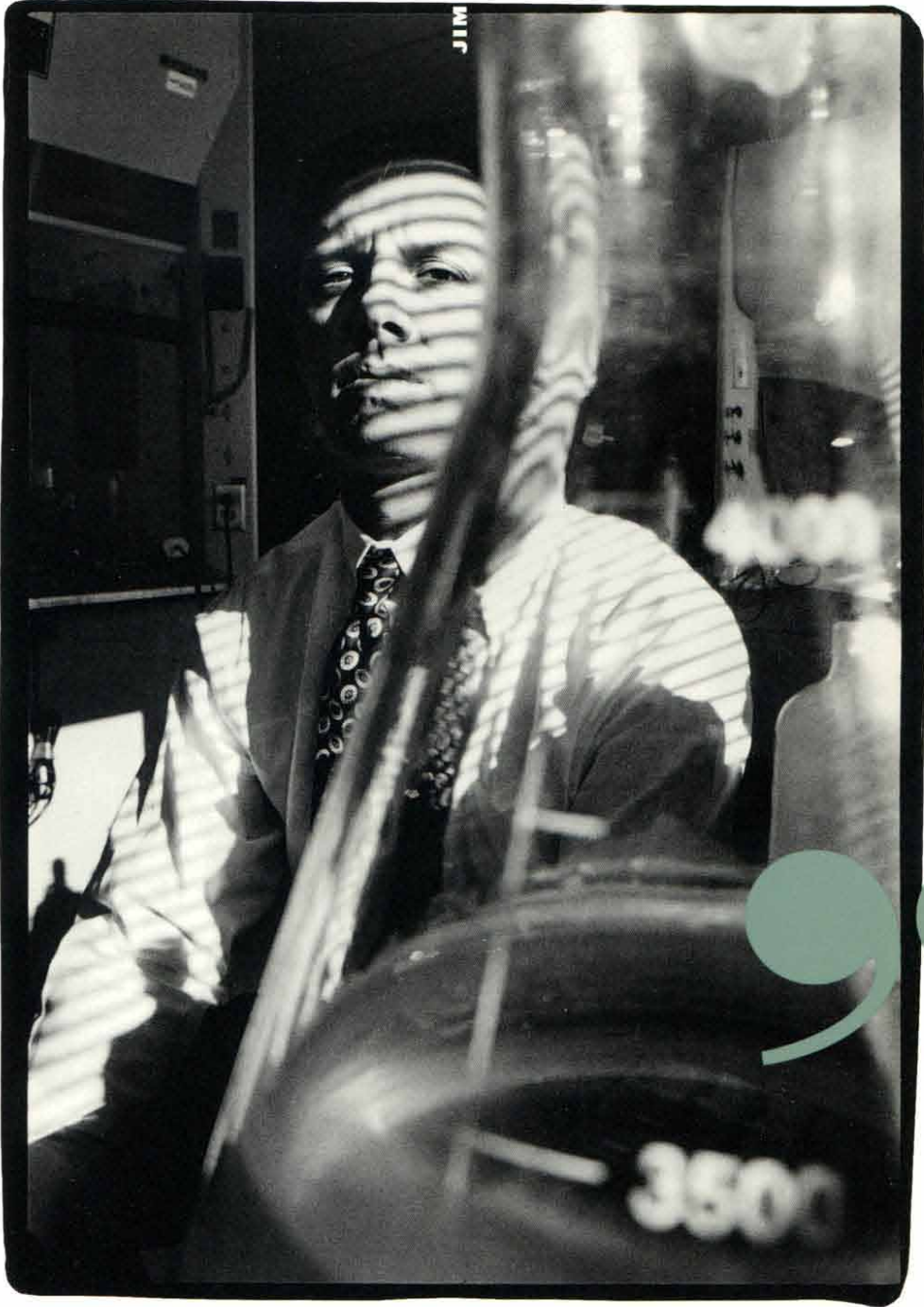
This facility is a two story, 62,739 square foot laboratory facility. Gillette is the sole tenant and uses this facility to develop and test its consumer products. Heavily trafficked with visitors, the space is modern and easily accessible.



Our acquisition strategy has always been a focused one, strategically identifying the key scientific centers of excellence and building a portfolio of properties within those hubs. This strategy has served us well, evidenced by strong growth we have achieved and the quality tenant base we attract.

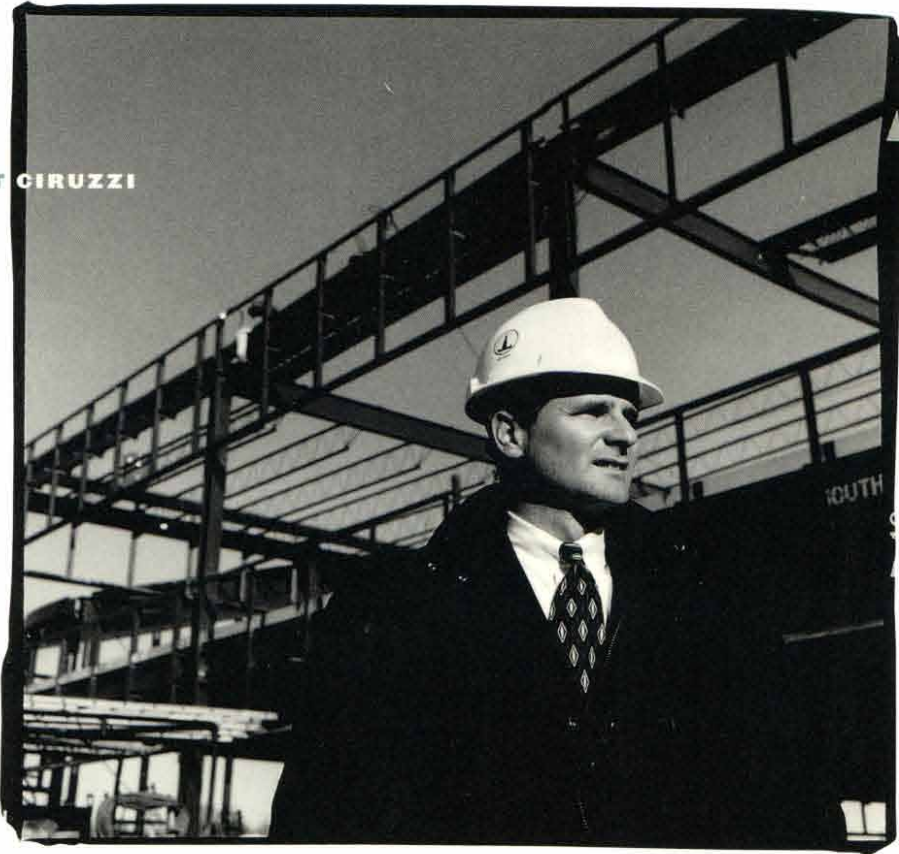
James H. Richardson
President
Alexandria Real Estate Equities, Inc.

JIM RICHARDSON





VINCENT CIRUZZI



Development

Development projects are true collaborative efforts between the architect, contractor, tenant and owner, in this case ARE. It is the only true way to be able to do a ground-up project that meets specific tenant requirements, while enhancing our franchise position in key scientific research hubs and fulfilling our business goals.

1201 CLOPPER ROAD, GAITHERSBURG, MARYLAND

Alexandria Research Center at Gaithersburg, Maryland consists of 348,000 square feet of laboratory and office development space on an 18.2 acre site. The Center will consist of four buildings. The first building, which has already been leased to Digene Corporation, a diagnostic products company, is 120,000 square feet. Construction is expected to be completed in late 1999, at which point Digene, who will be the sole tenant of the first building, will take occupancy.

Vincent Ciruzzi

Vice President - Construction and Development
Alexandria Real Estate Equities, Inc.

[ARE'S TARGET MARKETS]

ARE HAS IDENTIFIED TARGET MARKETS WHICH
WE BELIEVE ARE AMONG THE MOST DOMINANT HUBS
OF SCIENTIFIC RESEARCH IN THE UNITED STATES.

Prope

Suburban Washington D.C.

Eastern Massachusetts

New Jersey/Suburban Philadelphia

Southeast

San Francisco Bay

Seattle

San Diego

[FINANCIALS]

Real Estate Investments

[SELECTED FINANCIAL DATA]

ALEXANDRIA REAL ESTATE EQUITIES, INC.

THE FOLLOWING TABLE SHOULD BE READ IN CONJUNCTION
WITH OUR CONSOLIDATED FINANCIAL STATEMENTS AND
NOTES THERETO APPEARING ELSEWHERE IN THIS REPORT.

	YEAR ENDED DECEMBER 31				For the Period October 27, 1994 (inception) through December 31, 1994
	1998	1997	1996	1995	
<i>(Dollars in thousands, except per share amounts)</i>					
OPERATING DATA:					
Total revenue	\$ 61,016	\$ 34,846	\$ 17,673	\$ 9,923	\$ 1,011
Total expenses	41,613	37,643	15,498	9,057	1,659
Income (loss) from operations	19,403	(2,797)	2,175	866	(648)
Charge in lieu of taxes	-	-	-	(105)	-
Net income (loss)	<u>\$ 19,403</u>	<u>\$ (2,797)</u>	<u>\$ 2,175</u>	<u>\$ 761</u>	<u>\$ (648)</u>
Net income (loss) per share of common stock (pro forma for 1997, pro forma and restated for 1996, 1995 and 1994)					
-Basic	\$ 1.60	\$ (0.35)	\$ 0.60	\$ 0.43	\$ (0.37)
-Diluted	<u>\$ 1.58</u>	<u>\$ (0.35)</u>	<u>\$ 0.60</u>	<u>\$ 0.43</u>	<u>\$ (0.37)</u>
Weighted average shares of common stock outstanding (pro forma for 1997, pro forma and restated for 1996, 1995 and 1994) ⁽¹⁾					
-Basic	12,098,959	8,075,864	3,642,131	1,765,923	1,765,923
-Diluted	<u>12,306,470</u>	<u>8,075,864</u>	<u>3,642,131</u>	<u>1,765,923</u>	<u>1,765,923</u>
Cash dividends declared per share of common stock (pro forma for 1997, pro forma and restated for 1996 and 1995)	<u>\$ 1.60</u>	<u>\$ 1.60</u>	<u>\$ 0.87</u>	<u>\$ 0.51</u>	<u>\$ -</u>
BALANCE SHEET DATA (AT PERIOD END):					
Rental properties - net of accumulated depreciation	\$ 471,907	\$ 227,076	\$ 146,960	\$ 54,353	\$ 54,366
Total assets	\$ 530,296	\$ 248,454	\$ 160,480	\$ 58,702	\$ 56,600
Mortgage loans payable and unsecured line of credit	\$ 309,829	\$ 70,817	\$ 113,182	\$ 40,894	\$ 39,164
Total liabilities	\$ 330,527	\$ 81,537	\$ 120,907	\$ 42,369	\$ 40,119
Mandatorily redeemable Series V Preferred Stock	\$ -	\$ -	\$ 25,042	\$ -	\$ -
Stockholders' equity	<u>\$ 199,769</u>	<u>\$ 166,917</u>	<u>\$ 14,531</u>	<u>\$ 16,333</u>	<u>\$ 16,481</u>

For the
Period
October 27,
1994
(inception)
through
December
31, 1994

YEAR ENDED DECEMBER 31

(Dollars in thousands)

OTHER DATA:

	1998	1997	1996	1995	31, 1994
Net income (loss)	\$ 19,403	\$ (2,797)	\$ 2,175	\$ 761	\$ (648)
Add:					
Special bonus ⁽²⁾	—	353	—	—	—
Stock compensation ⁽³⁾	—	4,239	—	—	—
Post-retirement benefit ⁽⁴⁾	—	632	438	—	—
Acquisition LLC financing costs ⁽⁵⁾	—	6,973	—	—	—
Write-off of unamortized loan costs ⁽⁶⁾	—	2,295	—	—	—
Depreciation and amortization	10,296	4,866	2,405	1,668	63
Funds from operations ⁽⁷⁾	\$ 29,699	\$ 16,561	\$ 5,018	\$ 2,429	\$ (585)
Cash flows from operating activities	\$ 26,143	\$ 3,883	\$ (1,646)	\$ 355	\$ (1,024)
Cash flows from investing activities	\$ (246,753)	\$ (87,620)	\$ (94,900)	\$ (1,554)	\$ (29,924)
Cash flows from financing activities	\$ 220,104	\$ 84,101	\$ 97,323	\$ 927	\$ 32,139
Number of properties owned at period end	51	22	12	4	4
Rentable square feet of properties owned at period end	3,588,154	1,747,837	1,031,070	313,042	313,042
Occupancy of properties owned at period end	93%	97%	97%	96%	88%

(1) Pro forma shares of common stock outstanding for the years ended December 31, 1997 and 1996 include all shares outstanding after giving effect to the Offering, weighted for the period beginning from the date of the Offering, conversion of all series of preferred stock, the 1,765,923 to 1 stock split, the issuance of the stock grants and exercise of substitute stock options. Pro forma restated shares of common stock outstanding for the periods ended December 31, 1995 and 1994 also include shares outstanding after giving effect to the 1,765,923 to 1 stock split.

(2) Represents a \$353,000 special bonus we paid to an officer of Alexandria in 1997 in connection with the Offering.

(3) Represents an accrual for \$4,239,000 of non-recurring, non-cash compensation expense in 1997 relating to the issuance of stock options and stock grants. In connection with the Offering, the holders of options previously granted by Holdings under its 1994 stock option plans received options to purchase shares of our common stock in substitution for the Holdings options. These substitute options were exercised in connection with the Offering.

(4) This adjustment relates solely to the non-cash accrual of a one-time post-retirement benefit for an officer of Alexandria in 1997.

(5) In connection with the Offering, we acquired the membership interests in the Acquisition LLC for \$58,844,000. The purchase price we paid for the Acquisition LLC exceeded the cost incurred by the Acquisition LLC to purchase the properties it owned by \$6,973,000. This difference was accounted for as a financing cost.

(6) Of this amount, \$2,147,000 represents the write-off of costs associated with debt we paid off in connection with the Offering, and \$148,000 represents the write-off of costs associated with debt paid off in November 1997.

(7) We compute funds from operations ("FFO") in accordance with standards established by the Board of Governors of NAREIT in its March 1995 White Paper ("White Paper"). The White Paper defines FFO as net income (loss) (computed in accordance with GAAP), excluding gains (or losses) from debt restructuring and sales of property, and excluding amounts for extraordinary and non-recurring items, plus real estate related depreciation and amortization and after adjustments for unconsolidated partnerships and joint ventures. For a more detailed discussion of FFO, see "Management's Discussion and Analysis of Financial Condition and Results of Operations - Funds from Operations."

[MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS]

ALEXANDRIA REAL ESTATE EQUITIES, INC.

THE FOLLOWING DISCUSSION SHOULD BE READ IN CONJUNCTION
WITH OUR CONSOLIDATED FINANCIAL STATEMENTS AND
NOTES THERETO APPEARING ELSEWHERE IN THIS REPORT.

OVERVIEW

In June 1997, we completed an initial public offering of our common stock (the "Offering"). We issued 7,762,500 shares of our common stock in connection with the Offering (including shares issued in the related exercise of the underwriters' overallotment option) and raised \$138.9 million, net of underwriting discounts and commissions, advisory fees and offering costs.

Since the Offering, we have continued to devote substantially all of our resources to the acquisition, selective development and management of high quality, strategically located properties leased principally to tenants in the life science industry (we refer to these properties as "Life Science Facilities").

In 1998, we:

- Sold 1,150,000 shares of our common stock in May to PaineWebber Incorporated for inclusion in the PaineWebber Equity Trust REIT Series I, a unit investment trust. We received aggregate proceeds from this transaction, net of underwriting discounts and commissions, advisory fees and offering costs, of approximately \$32.7 million.
- Increased our borrowing capacity under our line of credit from \$150 million to \$250 million in August, thereby providing additional flexibility in pursuing acquisitions and funding tenant improvements and capital expenditures.
- Acquired a total of 29 properties with approximately 1.8 million in rentable square feet, including two properties aggregating approximately 105,000 rentable square feet that will undergo major renovation.

Our primary source of revenue is rental income and tenant recoveries from leases at the properties we own. Of the 51 properties we owned as of December 31, 1998, four were acquired in calendar year 1994, eight in 1996 (the "1996 Acquired Properties"), 10 in 1997 (the "1997 Acquired Properties") and 29 in 1998 (the "1998 Acquired Properties"). As a result of our acquisition activities, there were significant increases in total revenues and expenses for 1998 as compared to 1997.

RESULTS OF OPERATIONS

Comparison of the Year Ended December 31, 1998 to the Year Ended December 31, 1997

Rental revenue increased by \$22.9 million, or 89%, to \$48.5 million for 1998 compared to \$25.6 million for 1997. The increase resulted primarily from the 1997 Acquired Properties being owned for a full period and the addition of the 1998 Acquired Properties. A portion of the increase was due to \$277,000 in rental termination payments received in 1998 associated with leases at two of the properties. Rental revenue from the properties we acquired before January 1, 1997 (the "Same Properties") increased by \$234,000, or 1.6%, due to increases in rental rates and occupancy.

Tenant recoveries increased by \$2.9 million, or 35%, to \$11.3 million for 1998 compared to \$8.4 million for 1997. The increase resulted primarily from the 1997 Acquired Properties being owned for a full period and the addition of the 1998 Acquired Properties. Tenant recoveries for the Same Properties increased by \$149,000, or 2.8%, generally due to the improved identification and recovery of costs at certain properties.

Interest and other income increased by \$398,000, or 48%, to \$1.2 million for 1998 compared to \$836,000 for 1997, resulting primarily from \$511,000 of interest income from a \$6.0 million secured loan made in connection with the acquisition of one of the 1998 Acquired Properties. This increase was partially offset by a decrease in interest income resulting from a lower level of cash equivalents in 1998 compared to 1997, because cash equivalents had been used to acquire properties.

Rental operating expenses increased by \$4.6 million, or 52%, to \$13.4 million for 1998 compared to \$8.8 million for 1997. The increase resulted almost entirely from the 1997 Acquired Properties being owned for a full period and the addition of the 1998 Acquired Properties. Operating expenses for the Same Properties decreased by \$145,000, or 2.5%, primarily due to lower premiums on our blanket property and liability insurance policies.

The following is a comparison of property operating data computed under generally accepted accounting principles ("GAAP Basis") and under generally accepted accounting principles, adjusted to exclude the effect of straight line rent adjustments required by GAAP ("Cash Basis") for the Same Properties (in thousands, except percentage data):

	For the Year Ended December 31		Change
	1998	1997	
GAAP BASIS:			
Revenue	\$ 20,878	\$ 20,432	2.2%
Rental operating expenses	5,616	5,761	-2.5%
Net operating income	\$ 15,262	\$ 14,671	4.0%
CASH BASIS (1):			
Revenue	\$ 22,401	\$ 21,520	4.1%
Rental operating expenses	5,616	5,761	-2.5%
Net operating income	\$ 16,785	\$ 15,759	6.5%

(1) Revenue and operating expenses are computed in accordance with GAAP, except that revenue excludes the effect of straight line rent adjustments.

General and administrative expenses increased by \$1.4 million, or 56%, to \$3.9 million for 1998 compared to \$2.5 million for 1997 due to owning a larger portfolio of properties in 1998 compared to 1997 and increased costs incurred as a result of being a public company for a full year.

Interest expense increased by \$7.0 million, or 100%, to \$14.0 million for 1998 compared to \$7.0 million for 1997. The increase resulted from indebtedness incurred to acquire the 1997 Acquired Properties and the 1998 Acquired Properties, offset by a reduction in ongoing interest expense due to the payoff of \$72.7 million in secured notes payable in June 1997 with proceeds from the Offering.

Special bonus of \$353,000 in 1997 reflects a bonus we paid to an officer of Alexandria in connection with the Offering. Post retirement benefit expense of \$632,000 in 1997 reflects an adjustment for the non-cash accrual associated with a one-time post retirement benefit for an officer of Alexandria. Stock compensation expense of \$4.2 million was recorded in 1997 for the non-recurring, non-cash expense related to the stock grants and options we issued to our officers, directors and certain employees, principally in connection with the Offering.

Acquisition LLC financing costs of \$7.0 million in 1997 represent the portion of the purchase price of the membership interests in ARE Acquisitions, LLC (the "Acquisition LLC") in excess of the cost incurred by the Acquisition LLC to acquire its three Life Science Facilities.

Write-off of unamortized loan costs in 1997 represents the write-off of \$2.1 million in loan costs associated with \$72.7 million of secured notes we repaid with proceeds of the Offering and \$148,000 in loan costs associated with the payoff of debt in November 1997.

Depreciation and amortization increased by \$5.4 million, or 110%, to \$10.3 million for 1998 compared to \$4.9 million for 1997. The increase resulted primarily from depreciation associated with the 1997 Acquired Properties being owned for a full period and the addition of the 1998 Acquired Properties.

As a result of the foregoing, net income was \$19.4 million for 1998 compared to a net loss of \$2.8 million for 1997.

Comparison of the Year Ended December 31, 1997 to the Year Ended December 31, 1996

Rental revenue increased by \$12.7 million, or 98%, to \$25.6 million for 1997 compared to \$12.9 million for 1996. The increase resulted primarily from the 1996 Acquired Properties being owned for a full period and the addition of the 1997 Acquired Properties. Rental revenue from the properties we acquired before January 1, 1996 (the "1997 Same Properties") increased by \$180,000, or 2%. This increase resulted primarily from the conversion of 19,310 square feet of storage space to higher rent laboratory space at 10933 North Torrey Pines Road in October 1996.

Tenant recoveries increased by \$4.2 million, or 100%, to \$8.4 million for 1997 compared to \$4.2 million for 1996. The increase resulted primarily from the 1996 Acquired Properties being owned for a full period and the addition of the 1997 Acquired Properties. Tenant recoveries for the 1997 Same Properties increased by \$416,000, or 19%, due to an increase in operating expenses (particularly utilities) being passed through to the tenants.

Interest and other income increased by \$273,000, or 48%, to \$836,000 for 1997 compared to \$563,000 for 1996, resulting from an increase in interest income due to the investment of excess funds from the Offering and increased amounts in capital improvement reserve accounts.

Rental operating expenses increased by \$4.4 million, or 100%, to \$8.8 million for 1997 compared to \$4.4 million for 1996. The increase resulted almost entirely from the 1996 Acquired Properties being owned for a full period and the addition of the 1997 Acquired Properties. Operating expenses for the 1997 Same Properties increased by \$401,000, or 17%, primarily due to increased utility expenses (due to greater usage) which were passed through to the tenants.

General and administrative expenses increased by \$504,000, or 26%, to \$2.5 million for 1997 compared to \$2.0 million for 1996 due to our larger scope of operations and increased costs incurred as a result of being a public company.

Interest expense increased by \$716,000, or 11%, to \$7.0 million for 1997 compared to \$6.3 million for 1996. The increase resulted from indebtedness incurred to acquire the 1996 Acquired Properties and the 1997 Acquired Properties, offset by a reduction in ongoing interest expense due to the payoff of \$72.7 million in secured notes payable in June 1997 with proceeds from the Offering.

The amounts shown for special bonus, post-retirement benefit expense, stock compensation expense, Acquisition LLC financing costs and write-off unamortized loan costs in 1997 relate primarily to transactions associated with the Offering. We have described them in the prior section under " - Comparison of the Year Ended December 31, 1998 to the Year Ended December 31, 1997."

Depreciation and amortization increased by \$2.5 million, or 104%, to \$4.9 million for 1997 compared to \$2.4 million for 1996. The increase resulted primarily from depreciation associated with the 1996 Acquired Properties being owned for a full period and the addition of the 1997 Acquired Properties.

As a result of the foregoing, the net loss was \$2.8 million for 1997 compared to net income of \$2.2 million for 1996.

LIQUIDITY AND CAPITAL RESOURCES

Cash Flows

Net cash provided by operating activities for 1998 increased by \$22.2 million to \$26.1 million compared to \$3.9 million for 1997. The increase resulted primarily from operating cash flows from the addition of the 1997 Acquired Properties and the 1998 Acquired Properties.

Net cash used in investing activities increased by \$159.2 million to \$(246.8) million for 1998 compared to \$(87.6) million for 1997. The increase resulted from \$200.6 million used for the acquisition of the 1998 Acquired Properties, \$21.2 million used for additions to rental properties, \$18.9 million used for additions to land under development and \$6.0 million used for the addition of a note receivable made in connection with the acquisition of one of the 1998 Acquired Properties.

Net cash provided by financing activities increased by \$136.0 million to \$220.1 million for 1998 compared to \$84.1 million for 1997. This increase resulted from \$35.2 million in net proceeds from secured debt, \$171.0 million in borrowings under our unsecured line of credit, \$32.7 million in net proceeds from the issuance of our common stock and \$386,000 in net proceeds from the exercise of stock options, partially offset by payments of \$19.2 in dividends payable on our common stock.

Commitments

We are committed to complete the construction of a building and certain related improvements in San Diego, California at a remaining cost of approximately \$4.9 million under the terms of two leases. In addition, we are committed to complete the construction of a building and certain related improvements in Gaithersburg, Maryland at a remaining cost of between \$7.8 million and \$16.8 million (depending on the level of improvements to the facility elected by the tenant) under the terms of a lease. Under the terms of the lease, the tenant's rental rate will be adjusted depending on the ultimate cost of the improvements.

We are also committed to fund approximately \$11.1 million for investments in limited partnerships and rental properties, including the construction of tenant improvements under the terms of various leases. Of this amount, approximately \$3.2 million has been set aside in restricted cash accounts to complete the conversion of existing space into higher rent generic laboratory space (as well as certain related improvements) at 1102/1124 Columbia Street and 3000/3018 Western Avenue.

Restricted Cash

As of December 31, 1998, we had \$9.9 million in cash and cash equivalents, including \$7.5 million in restricted cash. Restricted cash consists of the following (in thousands):

	Amount
Reserve for tenant improvements established pursuant to leases at two of our properties ⁽¹⁾	\$ 3,220
Funds held in trust as additional security required under the terms of two of our secured notes payable	3,360
Security deposit funds based on the terms of certain lease agreements	911
	\$ 7,491

(1) Of this amount, \$2.1 million was returned to us in January 1999 upon the completion of tenant improvements at 3000/3018 Western Avenue.

Secured Debt

Secured debt as of December 31, 1998 consists of the following (dollars in thousands):

Collateral	Balance at December 31, 1998	Stated Interest Rate	Maturity Date
3535/3565 General Atomics Court, San Diego, CA	\$ 17,578	9.00%	December 2014
1431 Harbor Bay Parkway, Alameda, CA	8,500	7.165%	January 2014
1102/1124 Columbia Street, Seattle, WA	20,729	7.75%	May 2016
100/800/801 Capitola Drive, Durham, NC	12,547	8.68%	December 2006
14225 Newbrook Drive, Chantilly, VA and 3000/3018 Western Avenue, Seattle, WA	36,326	7.22%	May 2008
620 Memorial Drive, Cambridge, MA (1)	20,149	9.125%	May 2007
	\$ 115,829		

(1) The balance shown includes an unamortized premium of \$2,262 so that the effective rate of the loan is 7.25%.

The following is a summary of the scheduled principal payments for our secured debt as of December 31, 1998 (in thousands):

Year	Amount
1998	\$ 3,000
1999	2,907
2000	3,145
2001	3,395
2002	3,666
Thereafter	97,454
Subtotal	113,567
Unamortized premium	2,262
Total	\$ 115,829

Unsecured Line of Credit

Alexandria has an unsecured line of credit which provides for borrowings of up to \$250 million. Prior to August 1998, our line of credit provided for borrowings of up to \$150 million. Borrowings under the line of credit bear interest at a floating rate based on our election of either a LIBOR based rate or the higher of the bank's reference rate and the Federal Funds rate plus 0.5%. For each LIBOR based advance, we must elect to fix the rate for a period of one, two, three or six months.

The line of credit contains financial covenants, including, among other things, maintenance of minimum market net worth, a total liabilities to gross asset value ratio, and a fixed charge coverage ratio. In addition, the terms of the line of credit restrict, among other things, certain investments, indebtedness, distributions and mergers. Borrowings under the line of credit are limited to an amount based on a pool of unencumbered assets. Accordingly, as we acquire additional unencumbered properties, borrowings available under the line of credit will increase, but may not exceed \$250 million. As of December 31, 1998, borrowings under the line of credit were limited to approximately \$214,000,000, and carried a weighted average interest rate of 6.48%.

The line of credit expires May 31, 2000 and provides for annual extensions (provided there is no default) for two additional one-year periods upon notice by the company and consent of the participating banks.

In September 1998, we entered into an interest rate swap agreement with BankBoston N.A. (the "Bank") to hedge our exposure to variable interest rates associated with our line of credit. Interest paid is calculated at a fixed interest rate of 5.43% through May 31, 2000 on a notional amount of \$50 million and interest received is calculated at one month LIBOR. The net difference between the interest paid and the interest received is reflected as an adjustment to interest expense. The fair value of the swap agreement and changes in the fair value as a result of changes in market interest rates are not recognized in the financial statements.

Other Resources and Liquidity Requirements

On May 29, 1998, we sold 1,150,000 shares of our common stock to PaineWebber Incorporated for inclusion in the PaineWebber Equity Trust REIT Series I, a unit investment trust. The shares were issued at a price of \$30.5625 per share (before discounts and commissions) resulting in aggregate proceeds to us, net of offering costs of \$2.4 million, of approximately \$32.7 million.

We expect to continue meeting our short-term liquidity and capital requirements generally through our working capital and net cash provided by operating activities. We believe that the net cash provided by operating activities will continue to be sufficient to make distributions necessary to enable us to continue qualifying as a real estate investment trust. We also believe that net cash provided by operations will be sufficient to fund our recurring non-revenue enhancing capital expenditures, tenant improvements and leasing commissions.

We expect to meet certain long-term liquidity requirements, such as property acquisitions, property development activities, scheduled debt maturities, renovations, expansions and other non-recurring capital improvements, through long-term secured and unsecured indebtedness, including borrowings under the line of credit, and the issuance of additional debt and/or equity securities.

Exposure to Environmental Liabilities

In connection with the acquisition of all of our properties, we have obtained Phase I environmental assessments to ascertain the existence of any environmental liabilities or other issues. The Phase I environmental assessments of our properties have not revealed any environmental liabilities that we believe would have a material adverse effect on our financial condition or results of operations taken as a whole, nor are we aware of any material environmental liabilities.

CAPITAL EXPENDITURES, TENANT IMPROVEMENTS AND LEASING COSTS

The following table shows total and weighted average per square foot capital expenditures, tenant improvements and leasing costs (excluding capital expenditures and tenant improvements that are recoverable from tenants or are revenue enhancing) for the years ended December 31, 1998, 1997, 1996 and 1995, attributable to leases that commenced at our properties after our acquisition.

	Total/ Weighted Average	1998	1997	1996	1995
CAPITAL EXPENDITURES:					
Weighted average square feet in portfolio	5,112,759	2,891,863	1,342,216	563,901	314,779
Property related capital expenditures	\$ 1,086,000	\$ 341,000	\$ 547,000	\$ 181,000	\$ 17,000
Per weighted average square foot in portfolio	\$ 0.21	\$ 0.12	\$ 0.41	\$ 0.32	\$ 0.05
TENANT IMPROVEMENTS AND LEASING COSTS:					
<i>Retenanted space:</i>					
Retenanted square feet	359,470	88,181	40,953	180,398	49,938
Tenant improvements and leasing costs	\$ 2,438,000	\$ 478,000	\$ 164,000	\$ 1,220,000	\$ 576,000
Per square foot leased	\$ 6.78	\$ 5.42	\$ 4.00	\$ 6.76	\$ 11.53
<i>Renewal space:</i>					
Renewal square feet	119,417	77,038	1,232	25,063	16,084
Tenant improvements and leasing costs	\$ 117,000	\$ 69,000	\$ -	\$ -	\$ 48,000
Per square foot leased	\$ 0.98	\$ 0.90	\$ -	\$ -	\$ 2.98

Capital expenditures fluctuate in any given period due to the nature, extent, and timing of improvements required and the extent to which they are recoverable from our tenants. We maintain an active preventive maintenance program at each of our properties to minimize required capital improvements.

Tenant improvements and leasing costs also fluctuate in any given year depending upon factors such as the timing and extent of vacancies, the type of lease (renewal tenant or retenanted space), the involvement of external leasing agents and overall competitive market conditions.

INFLATION

As of December 31, 1998, approximately 78% of our leases (on a square footage basis) were triple net leases, requiring tenants to pay substantially all real estate taxes and insurance, common area and other operating expenses (including increases thereto). In addition, approximately 17% of our leases (on a square footage basis) required the tenants to pay a majority of operating expenses. Approximately 83% of our leases (on a square footage basis) contain effective annual rent escalations that are either fixed (ranging from 2.5% to 4.0%) or indexed based on the consumer price index or other index. Accordingly, we do not believe that our earnings or cash flow are subject to any significant risk of inflation. An increase in inflation, however, could result in an increase in our variable rate borrowing cost, including borrowings under the unsecured line of credit.

IMPACT OF THE YEAR 2000

The year 2000 issue is the result of computer programs being written using two digits rather than four digits to define the applicable year. Any of our computer programs that have time-sensitive software may recognize a date using "00" as the year 1900 rather than the year 2000. This could result in a system failure or miscalculations causing disruptions of operations, including, among other things, a temporary inability to process transactions, send tenant invoices, provide building services or engage in similar normal business activities.

We rely on computer technologies to operate our business. In October 1998, we formed an internal task force to identify, assess and evaluate our critical systems to determine which year 2000 related problems may cause system errors or failures. We have identified three major areas as critical systems: (i) internal accounting systems, (ii) systems of significant tenants, vendors and financial institutions; and (iii) internal building systems at our properties. We have engaged consulting professionals from a nationally recognized accounting firm to review our plans and assist us with our solutions.

The following discussion of our year 2000 project contains numerous forward-looking statements based on inherently uncertain

information. The cost of our evaluation and the date on which we plan to complete our internal evaluation and related remediation projects are based on our best estimates. We derived these estimates using a number of assumptions of future events, including the continued availability of internal and external resources, third-party modifications and other factors. However, there can be no guarantee that these estimates will be achieved, and actual results may be materially different from those anticipated. Moreover, although we believe that we will be operating in a year 2000 compliant manner prior to December 31, 1999, there can be no assurance that any failure to modify a critical system would not have a material adverse effect on our operations.

Readiness

Our year 2000 project is designed to ensure that all critical systems have been evaluated and will be suitable for continued use into and beyond the year 2000. We expect to have completed our identification and initial evaluation of critical systems in the first quarter of 1999, and we expect we will have implemented substantially all of the necessary remedial actions by mid-1999.

We have completed our review of our internal accounting systems. Our most significant accounting systems, our general ledger system and our accounts payable system, are currently year 2000 compliant. The systems have been tested and we do not anticipate year 2000 problems. Our billing system is currently not year 2000 compliant. We have been notified by the vendor that they will be distributing the year 2000 compliant upgrade to the software at no additional cost by June 1999. Once we receive this upgrade, the software will be tested for compatibility and year 2000 compliance.

We place a high degree of reliance on computer systems of third parties, such as tenants, vendors and financial institutions. Although we are assessing the readiness of these third parties, there can be no guarantee that the failure of these third parties to modify their systems in advance of December 31, 1999 would not have a material adverse effect on our operations. We have surveyed our most significant third-party vendors and financial institutions, and all surveyed indicated that they have implemented year 2000 programs. We are currently in the process of surveying all major vendors and suppliers for their year 2000 readiness. In addition, we are in the process of surveying our significant tenants for their year 2000 readiness and expect to complete such tenant assessments in the first quarter of 1999. We are continually participating in such surveys with new tenants, vendors and other third-party suppliers. If future risk assessments of third-party suppliers or tenants indicate significant exposure from a supplier's year 2000 problem, such supplier or tenant will be asked to demonstrate how such problems will be addressed. We believe that we have viable alternatives for each of our major vendors.

The final critical system the task force is evaluating consists of internal systems in our properties that may have embedded microprocessors with potential year 2000 problems, mainly building systems, including heating, ventilation and air conditioning systems, elevators and security systems. We are in the process of identifying the areas and systems that use embedded microprocessors and will determine whether any modification or replacement is necessary. We anticipate using the services of outside experts to assist us with this phase of our year 2000 project. The evaluation of these areas is in process and is expected to be completed in the first quarter of 1999, and any required modifications are expected to be made by mid-1999.

Cost

We do not expect our year 2000 project costs, including the costs of any remedial activities and outside experts, to be material. The aggregate cost of purchasing conversion packages for the accounting systems and the cost to survey tenants, vendors and financial institutions are not expected to be material. In addition, any costs incurred to replace or upgrade building systems will constitute property maintenance costs, and are therefore generally recoverable from the tenants pursuant to the terms of their existing leases.

Risks

We believe that the principal risks associated with the year 2000 issue include the risk of disruption of our operations due to operational failures of third parties, including tenants, vendors and financial institutions, and the risk of business interruption due to building system failures. We do not believe that the risk of disruptions due to operational failures of vendors or financial institutions is significant, because our major vendors and financial institutions are currently year 2000 compliant, and we believe we have viable alternatives for such suppliers. If any of our major tenants do not become year 2000 compliant on schedule, such tenant's operations and financial condition could be adversely affected, which may impact the tenant's ability to meet its rent obligations. Similarly, if our building systems failed due to year 2000 problems, services to our properties and tenants, such as mechanical and security services, could be interrupted, resulting in potential rent disputes with the tenants. We believe, however, that our early involvement in identifying, assessing and evaluating our critical systems should minimize the risk of year 2000 problems to our operations.

Contingency Plans

We believe that development of contingency plans for significant exposures to potential year 2000 problems are integral to our planning process. Once we have completed our identification and evaluation of critical systems and have completed the subsequent remedial action phase, we will again assess our exposure to year 2000 problems. Based on this assessment, we intend to develop appropriate contingency plans for the systems. Because we anticipate being substantially year 2000 compliant by mid-1999, we believe that adequate time exists to ensure that alternatives can be developed, assessed and implemented prior to the end of 1999. Based on our assessment of the success or adequacy of these alternatives, we intend to develop contingency plans. We cannot give assurance, however, that failure to develop an alternative or an appropriate contingency plan would not have a material adverse effect on our operations.

FUNDS FROM OPERATIONS

We believe that funds from operations ("FFO") is helpful to investors as a measure of the performance of an equity REIT because, along with cash flows from operating activities, financing activities and investing activities, it provides investors with an understanding of our ability to incur and service debt, to make capital expenditures and to make distributions. We compute FFO in accordance with standards established by the Board of Governors of the National Association of Real Estate Investment Trusts ("NAREIT") in its March 1995 White Paper (the "White Paper"), which may differ from the methodology for calculating FFO utilized by other equity REITs, and, accordingly, may not be comparable to such other REITs. Further, FFO does not represent amounts available for our discretionary use because of needed capital replacement or expansion, debt service obligations, or other commitments and uncertainties. The White Paper defines FFO as net income (loss) (computed in accordance with generally accepted accounting principals ("GAAP")), excluding gains (or losses) from debt restructuring and sales of property, and excluding amounts for extraordinary and non-recurring items, plus real estate related depreciation and amortization and after adjustments for unconsolidated partnerships and joint ventures. FFO should not be considered as an alternative to net income (determined in accordance with GAAP) as an indication of our financial performance or to cash flows from operating activities (determined in accordance with GAAP) as a measure of our liquidity, nor is it indicative of funds available to fund our cash needs, including our ability to make distributions. (See "-Cash Flows" for information regarding these measures of cash flow).

The following table presents our FFO for the years ended December 31, 1998, 1997 and 1996 (in thousands):

	YEAR ENDED DECEMBER 31		
	1998	1997	1996
OPERATING DATA:			
Net income (loss)	\$ 19,403	\$ (2,797)	\$ 2,175
Add:			
Special bonus	—	353	—
Stock compensation	—	4,239	—
Post-retirement benefit	—	632	438
Acquisition LLC financing costs	—	6,973	—
Write-off of unamortized loan costs	—	2,295	—
Depreciation and amortization	10,296	4,866	2,405
Funds from Operations	\$ 29,699	\$ 16,561	\$ 5,018

PROPERTY AND LEASE INFORMATION

The following table is a summary of our property portfolio as of December 31, 1998 (dollars in thousands):

REGION:	Number of Properties	Rentable Square Feet	Annualized Base Rent	Occupancy Percentage
Suburban Washington D.C.	17	1,533,833	\$ 20,917	94.5% (1)
California – San Diego	7	428,955	11,529	98.9%
California – San Francisco Bay	6	355,398	5,364	91.4% (1)
Southeast	4	255,977	3,661	99.1% (1)
New Jersey/Suburban Philadelphia	5	273,048	3,497	100.0%
Eastern Massachusetts	5	278,927	7,724	100.0%
Washington – Seattle	3	328,556	8,727	96.7%
Subtotal	47	3,454,694	61,419	96.2%
Renovation/Repositioning Properties	4	133,460	88	7.3%
Total	51	3,588,154	\$ 61,507	92.9%

(1) All, or substantially all, of the vacant space is office or warehouse space.

The following table shows certain information with respect to the lease expirations of our properties as of December 31, 1998:

Year of Lease Expiration	Number of Expiring Leases	Square Footage of Expiring Leases	Percentage of Aggregate Portfolio Lease Square Foot	Annualized Base Rent of Expiring Leases (per square foot)
1999	47	332,161	10.0%	\$ 18.08
2000	26	383,600	11.5%	\$ 16.89
2001	22	424,382	12.7%	\$ 18.93
2002	11	118,086	3.5%	\$ 14.25
2003	17	366,782	11.0%	\$ 15.46
Thereafter	35	1,706,942	51.5%	\$ 19.43

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk is the exposure to loss resulting from changes in interest rates, foreign currency exchange rates, commodity prices and equity prices. The primary market risk to which we are exposed is interest rate risk, which is sensitive to many factors, including governmental monetary and tax policies, domestic and international economic and political considerations and other factors that are beyond our control.

In order to modify and manage the interest characteristics of our outstanding debt and limit the effects of interest rates on our operations, we may utilize a variety of financial instruments, including interest rate swaps, caps, floors and other interest rate exchange contracts. The use of these types of instruments to hedge our exposure to changes in interest rates carries additional risks such as counter-party credit risk and legal enforceability of hedging contracts.

Our future earnings, cash flows and fair values relating to financial instruments are primarily dependent upon prevalent market rates of interest, such as LIBOR. However, due to the purchase of our interest rate swap agreement, the effects of interest rate changes are reduced. Based on interest rates at December 31, 1998, a 1% increase in interest rates on our line of credit would decrease annual future earnings and cash flows, after considering the effect of our interest rate swap agreement, by approximately \$1.4 million. A 1% decrease in interest rates on our line of credit would increase annual future earnings and cash flows, after considering the effect of our interest rate swap agreement, by approximately \$1.4 million. A 1% increase in interest rates on our secured debt and interest rate swap agreement would increase their fair value by approximately \$7.7 million. A 1% decrease in interest rates on our secured debt and interest rate swap agreement would increase their fair value by approximately \$8.8 million. A 1% increase or decrease in interest rates on our second note receivable would not have a material impact on its fair value.

These amounts are determined by considering the impact of the hypothetical interest rates on our borrowing cost and interest rate swap agreement. These analyses do not consider the effects of the reduced level of overall economic activity that could exist in such an environment. Further, in the event of a change of such magnitude, we would consider taking actions to further mitigate our exposure to the change. However, due to the uncertainty of the specific actions that would be taken and their possible effects, the sensitivity analysis assumes no changes in our capital structure.

[CONSOLIDATED BALANCE SHEETS]

ALEXANDRIA REAL ESTATE EQUITIES, INC. AND SUBSIDIARIES

(Dollars in thousands, except per share amounts)

ASSETS

Rental properties, net
 Land under development
 Cash and cash equivalents
 Tenant security deposits and other restricted cash
 Secured note receivable
 Tenant receivables and deferred rent
 Other assets
 Total assets

LIABILITIES AND STOCKHOLDERS' EQUITY

Secured notes payable (includes unamortized premium of \$2,262 in 1998)
 Unsecured line of credit
 Accounts payable, accrued expenses and tenant security deposits
 Dividends payable

Commitments and contingencies

Stockholders' equity:

Common stock, \$0.01 par value per share, 100,000,000 shares
 authorized; 12,586,263 and 11,404,631 shares issued and outstanding
 at December 31, 1998 and 1997, respectively
 Additional paid-in capital
 Retained earnings (accumulated deficit)

Total stockholders' equity

Total liabilities and stockholders' equity

DECEMBER 31

	1998	1997
	\$ 471,907	\$ 227,076
	21,839	2,894
	1,554	2,060
	7,491	6,799
	6,000	-
	8,479	3,630
	13,026	5,995
	\$ 530,296	\$ 248,454
	\$ 115,829	\$ 47,817
	194,000	23,000
	15,663	6,158
	5,035	4,562
	330,527	81,537
	-	-
	126	114
	199,643	173,735
	-	(6,932)
	199,769	166,917
	\$ 530,296	\$ 248,454

See accompanying notes.

[CONSOLIDATED STATEMENTS OF OPERATIONS]

ALEXANDRIA REAL ESTATE EQUITIES, INC. AND SUBSIDIARIES

(Dollars in thousands, except per share amounts)

REVENUES:

Rental
 Tenant recoveries
 Interest and other income

EXPENSES:

Rental operations
 General and administrative
 Interest
 Stock compensation
 Post retirement benefit
 Special bonus
 Acquisition LLC financing costs
 Write-off of unamortized loan costs
 Depreciation and amortization

Net income (loss)

Net income allocated to preferred stockholders

Net income (loss) allocated to common stockholders

Net income (loss) per share of common stock (pro forma for 1997,
 pro forma and restated for 1996):

– Basic
 – Diluted

Weighted average shares of common stock outstanding (pro forma
 for 1997, pro forma and restated for 1996):

– Basic
 – Diluted

	YEAR ENDED DECEMBER 31		
	1998	1997	1996
	\$ 48,469	\$ 25,622	\$ 12,941
	11,313	8,388	4,169
	1,234	836	563
	<u>61,016</u>	<u>34,846</u>	<u>17,673</u>
	13,390	8,766	4,356
	3,894	2,476	1,972
	14,033	7,043	6,327
	–	4,239	–
	–	632	438
	–	353	–
	–	6,973	–
	–	2,295	–
	10,296	4,866	2,405
	<u>41,613</u>	<u>37,643</u>	<u>15,498</u>
	<u>\$ 19,403</u>	<u>\$ (2,797)</u>	<u>\$ 2,175</u>
	<u>\$ –</u>	<u>\$ 3,038</u>	<u>\$ 1,590</u>
	<u>\$ 19,403</u>	<u>\$ (5,835)</u>	<u>\$ 585</u>
	\$ 1.60	\$ (0.35)	\$ 0.60
	\$ 1.58	\$ (0.35)	\$ 0.60
	12,098,959	8,075,864	3,642,131
	<u>12,306,470</u>	<u>8,075,864</u>	<u>3,642,131</u>

See accompanying notes.

[CONSOLIDATED STATEMENTS OF CASH FLOWS]

ALEXANDRIA REAL ESTATE EQUITIES, INC. AND SUBSIDIARIES

(Dollars in thousands)	YEAR ENDED DECEMBER 31		
	1998	1997	1996
OPERATING ACTIVITIES			
Net income (loss)	\$ 19,403	\$ (2,797)	\$ 2,175
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:			
Depreciation and amortization	10,296	4,866	2,405
Stock option compensation	-	4,161	-
Changes in operating assets and liabilities:			
Tenant security deposits and other restricted cash	(692)	(1,214)	(4,371)
Tenant receivables and deferred rent	(4,849)	(2,298)	(502)
Other assets	(7,520)	(1,343)	(3,633)
Accounts payable, accrued expenses and tenant security deposits	9,505	2,508	2,280
Net cash provided by (used in) operating activities	26,143	3,883	(1,646)
INVESTING ACTIVITIES			
Purchase of rental properties	(200,590)	(81,160)	(93,322)
Additions to rental properties	(21,218)	(3,566)	(1,578)
Additions to land under development	(18,945)	(2,894)	-
Issuance of note receivable	(6,000)	-	-
Net cash used in investing activities	(246,753)	(87,620)	(94,900)
FINANCING ACTIVITIES			
Proceeds from secured notes payable	36,500	15,360	77,260
Net proceeds from issuances of common stock	32,713	138,919	-
Exercise of stock options	386	-	-
Proceeds from issuance of Series V preferred stock (net of issuance costs of \$3,391)	-	-	24,109
Proceeds from issuance of Series U preferred stock	-	-	110
Proceeds from unsecured line of credit	171,000	25,500	-
(Decrease) increase in due to Health Science Properties Holding Corporation	-	(2,525)	2,420
Principal reductions on unsecured line of credit	-	(2,500)	(4,000)
Principal reductions on secured notes payable	(1,318)	(80,725)	(972)
Common dividends paid	(19,177)	(8,800)	(939)
Preferred dividends paid	-	(1,127)	(665)
Redemption of Series T preferred stock	-	(1)	-
Net cash provided by financing activities	220,104	84,101	97,323
Net (decrease) increase in cash and cash equivalents	(506)	364	777
Cash and cash equivalents at beginning of year	2,060	1,696	919
Cash and cash equivalents at end of year	\$ 1,554	\$ 2,060	\$ 1,696
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION			
Cash paid during the year for interest and financing costs, net of interest capitalized	\$ 12,778	\$ 13,552	\$ 5,953

See accompanying notes.

[CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY]

ALEXANDRIA REAL ESTATE EQUITIES, INC. AND SUBSIDIARIES

<i>(Dollars in thousands)</i>	Number of Series T Preferred Shares	Series T Preferred Stock	Number of Series U Preferred Shares
Balance at January 1, 1996 (restated)	12	\$ 1	-
Issuance of Series U preferred stock	-	-	220
Accretion on Series V preferred stock	-	-	-
Cash dividends on Series T, U, & V preferred stock	-	-	-
Dividends declared on common stock	-	-	-
Net income	-	-	-
Balance at December 31, 1996 (restated)	12	1	220
Accretion on Series V preferred stock	-	-	-
Cash dividends on Series T, U and V preferred stock	-	-	-
Exercise of compensatory stock options and issuance of stock grants (including compensation expense of \$4,161)	-	-	-
Issuance of common stock in connection with initial public offering, net of offering costs	-	-	-
Conversion of Series V and Series U preferred stock	-	-	(220)
Redemption of Series T preferred stock	(12)	(1)	-
Dividends declared on common stock	-	-	-
Net loss	-	-	-
Balance at December 31, 1997	-	-	-
Issuance of common stock, net of offering costs	-	-	-
Exercise of stock options, net	-	-	-
Dividends declared on common stock	-	-	-
Net income	-	-	-
Balance at December 31, 1998	-	\$ -	-

See accompanying notes.

	Series U Preferred Stock	Number of Common Shares	Common Stock	Additional Paid-in Capital	Accumulated Deficit	Total
\$	-	1,765,923	\$ 18	\$ 17,110	\$ (796)	\$ 16,333
	110	-	-	-	-	110
	-	-	-	(933)	-	(933)
	-	-	-	-	(665)	(665)
	-	-	-	-	(2,489)	(2,489)
	-	-	-	-	2,175	2,175
	110	1,765,923	18	16,177	(1,775)	14,531
	-	-	-	(1,911)	-	(1,911)
	-	-	-	-	(1,127)	(1,127)
	-	209,615	2	4,190	-	4,192
	-	7,762,500	78	138,812	-	138,890
	(110)	1,666,593	16	27,045	-	26,951
	-	-	-	-	-	(1)
	-	-	-	(10,578)	(1,233)	(11,811)
	-	-	-	-	(2,797)	(2,797)
	-	11,404,631	114	173,735	(6,932)	166,917
	-	1,150,000	12	32,701	-	32,713
	-	31,632	-	386	-	386
	-	-	-	(7,179)	(12,471)	(19,650)
	-	-	-	-	19,403	19,403
\$	-	12,586,263	\$ 126	\$ 199,643	\$ -	\$ 199,769

One

BACKGROUND

Alexandria Real Estate Equities, Inc. is a real estate investment trust ("REIT") formed in 1994. We are engaged primarily in the acquisition, management, and selective development of properties for lease principally to participants in the life science industry (we refer to these properties as "Life Science Facilities"). As of December 31, 1998, our portfolio consisted of 51 properties in nine states with approximately 3,588,000 rentable square feet, compared to 22 properties in four states with approximately 1,748,000 rentable square feet as of December 31, 1997.

On June 2, 1997, we completed our initial public offering (the "Offering") of 6,750,000 shares of common stock. The Offering price was \$20.00 per share, resulting in gross proceeds of \$135,000,000. On June 26, 1997, the underwriters exercised their over-allotment option provided for in the Offering, and we issued an additional 1,012,500 shares of common stock, resulting in additional gross proceeds of \$20,250,000. The aggregate net proceeds of the Offering (including exercise of the over-allotment option), net of underwriting discounts and commissions, advisory fees and offering costs, were approximately \$138,890,000.

The following transactions also occurred in June 1997 in connection with the Offering:

- We repaid debt of approximately \$77,723,000, including (i) mortgage debt of \$72,698,000, (ii) debt of \$2,500,000 outstanding under our prior unsecured line of credit, and (iii) debt of \$2,525,000 to Health Science Properties Holding Corporation ("Holdings"). Holdings owned all of our common stock prior to the Offering and 14% of our common stock as of December 31, 1998.
- We obtained two new mortgage loans totaling \$15,360,000.
- We acquired an entity that owns three Life Science Facilities from affiliates of PaineWebber Incorporated, the lead managing underwriter for the Offering, for an aggregate purchase price of \$58,844,000 (see Note 12).
- Each previously outstanding share of our common stock was split into 1,765,923 shares of common stock. The share data as of and for the year ended December 31, 1996 has been restated to reflect the effects of the stock split.
- All of the previously outstanding shares of Series T preferred stock were redeemed at their stated value (\$1,200 in the aggregate) (see Note 9).

- All of the previously outstanding shares of Series U preferred stock and Series V preferred stock were converted into shares of common stock (7,354 shares in the aggregate for Series U and 1,659,239 shares in the aggregate for Series V) (see Notes 8 and 9).
- Officers, directors and certain employees of Alexandria were granted an aggregate of 152,615 shares of our common stock. In addition, our officers, directors and certain employees were granted options to purchase 57,000 shares of our common stock in substitution for stock options previously issued by Holdings (see Notes 8 and 11). These options were exercised at a nominal exercise price in connection with the Offering.
- Officers, directors and employees of Alexandria were granted options under the 1997 stock option plan to purchase an aggregate of 600,000 shares of our common stock at the Offering price (see Note 11).
- A special bonus of \$353,000 was paid to an officer of Alexandria.

Two

BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The consolidated financial statements include the accounts of Alexandria and its subsidiaries. All significant intercompany balances and transactions have been eliminated.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash Equivalents

We consider all highly liquid investments with original maturities of three months or less when purchased to be cash equivalents.

Reclassifications

Certain prior year amounts have been reclassified to conform to the current year presentation.

Rental Properties and Land Under Development

Properties and land under development are stated at the lower of cost or estimated fair value. Write-downs to estimated fair value would be recognized when impairment indicators are present and a property's estimated undiscounted future cash flows, before interest charges, are less than its book value. In that situation, we would recognize an impairment loss to the extent the carrying amount exceeds the fair value of the property. Based on our assessment, no write-downs to estimated fair value were necessary for the periods presented.

The cost of maintenance and repairs is expensed as incurred. Major replacements and betterments are capitalized and depreciated over their estimated useful lives.

Depreciation is provided using the straight-line method using estimated lives of 30 to 40 years for buildings and building improvements, 20 years for land improvements, and the term of the respective lease for tenant improvements.

Restricted Cash

Restricted cash consists of the following (in thousands):

	DECEMBER 31	
	1998	1997
Reserve for tenant improvements established pursuant to leases at two of our properties	\$ 3,220	\$ 3,364
Funds held in trust as additional security required under the terms of two of our secured notes payable	3,360	1,966
Security deposit funds based on the terms of certain lease agreements	911	1,469
	<u>\$ 7,491</u>	<u>\$ 6,799</u>

Loan Fees and Costs

Fees and costs incurred in obtaining long-term financing are amortized over the terms of the related loans and included in interest expense. Loan fees and costs, net of related amortization, totaled \$3,424,000 and \$1,350,000 as of December 31, 1998 and 1997, respectively.

Rental Income

Rental income from leases with scheduled rent increases, free rent and other rent adjustments are recognized on a straight-line basis over the respective lease term. We include amounts currently recognized as income, and expected to be received in later years, in tenant receivables and deferred rent on our consolidated balance sheet. Amounts received currently, but recognized as income in future years, are included in unearned rent on our consolidated balance sheet.

Other Income

Other income consists of interest income and other income associated with the operations of the properties. Interest income was \$978,000, \$588,000 and \$118,000 in 1998, 1997 and 1996, respectively.

Leasing Commissions

Leasing commissions are amortized on a straight-line basis over the term of the related lease. Leasing commissions, net of related amortization, totaled \$4,856,000 and \$847,000 as of December 31, 1998 and 1997, respectively.

Fair Value of Financial Instruments

The carrying amount of cash and cash equivalents approximates fair value because their maturity is less than three months. The carrying amount of our secured note receivable approximates fair value because the applicable interest rate approximates the market rate for this loan.

The fair value of our secured notes payable was estimated using discounted cash flows analyses based on borrowing rates we believe we could obtain with similar terms and maturities. As of December 31, 1998 and 1997, the fair value of our secured notes payable was approximately \$118,310,000 and \$46,822,000, respectively.

Net Income (Loss) Per Share

Historical per share data has not been presented for 1997 and 1996 because it is not meaningful due to the material changes in our capital structure as a result of the Offering. Instead, we have presented net income (loss) per share for these years on a pro forma basis, giving effect to the Offering and related transactions.

Pro forma shares of common stock outstanding for the years ended December 31, 1997 and 1996 include all shares outstanding after giving effect to the 1,765,923 to 1 stock split, the issuance of stock grants, the issuance and exercise of substitute stock options and the conversion of the Series U and Series V preferred stock. In addition, shares issued to the public in connection with the Offering have been weighted for the period of time they were outstanding.

We have adopted Statement of Financial Accounting Standards No. 128, "Earnings per Share," and have restated pro forma net income per share for the year ended December 31, 1996. Basic and diluted net income per share are the same for 1997 because the stock options outstanding as of December 31, 1997 were antidilutive. There were no dilutive stock options on a pro forma basis for 1996.

The following table shows the computation of net income (loss) per share of common stock outstanding:

	YEAR ENDED DECEMBER 31		
	1998	1997	1996
<i>(Dollars in thousands, except per share amounts)</i>			
Net income (loss)	\$ 19,403	\$ (2,797)	\$ 2,175
Weighted average shares – basic (pro forma for 1997, pro forma and restated for 1996)	12,098,959	8,075,864	3,642,131
Add: dilutive effect of stock options	207,511	–	–
Weighted average shares – diluted (pro forma for 1997, pro forma and restated for 1996)	12,306,470	8,075,864	3,642,131
Net income (loss) per share – basic (pro forma for 1997, pro forma and restated for 1996)	\$ 1.60	\$ (0.35)	\$ 0.60
Net income (loss) per share – diluted (pro forma for 1997, pro forma and restated for 1996)	\$ 1.58	\$ (0.35)	\$ 0.60
Dividends declared per share (pro forma for 1997, pro forma and restated for 1996)	\$ 1.60	\$ 1.60	\$ 0.87

Operating Segments

In June 1997, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 131, "Disclosures About Segments of an Enterprise and Related Information," which is effective for years beginning after December 15, 1997. Statement 131 establishes standards for the way that public business enterprises report information about operating segments. Statement 131 also establishes standards for related disclosure about products and services, geographic areas, and major customers. Since we operate as a single segment, the implementation of Statement 131 did not have an impact on how we report our results of operations.

Income Taxes

As a REIT, we are not subject to federal income taxation as long as we meet a number of organizational and operational requirements and distribute all of our taxable income to our stockholders. Since we believe we have met these requirements and our distributions exceeded taxable income, no federal income tax provision has been reflected in the accompanying consolidated financial statements for the years ended December 31, 1998, 1997 and 1996. If we fail to qualify as a REIT in any taxable year, we will be subject to federal income tax on our taxable income at regular corporate tax rates. For the years ended December 31, 1998 and 1996, we reported that none of our distributions with respect to common stock represented a return of capital for federal income tax purposes. For the year ended December 31, 1997, we reported that 37.6% of our distributions with respect to common stock represented a return of capital.

Three

RENTAL PROPERTIES

Rental properties are as follows (in thousands):

	DECEMBER 31	
	1998	1997
Land	\$ 76,254	\$ 43,485
Building and improvements	393,728	189,528
Tenant and other improvements	20,536	2,867
	490,518	235,880
Less accumulated depreciation	(18,611)	(8,804)
	\$ 471,907	\$ 227,076

Nine of the rental properties are encumbered by deeds of trust and assignments of rents and leases associated with the properties (see Note 6). The net book value of these properties as of December 31, 1998 is \$174,185,000.

We lease space under noncancelable leases with remaining terms of one to 18 years.

A majority of our leases require that the lessee pay all taxes, maintenance, insurance and certain other operating expenses applicable to the leased properties.

We capitalize interest to properties under construction and renovation during the period the asset is undergoing activities to prepare it for its intended use. Total interest capitalized for the years ended December 31, 1998 and 1997 was \$2,199,000 and \$96,000, respectively. Total interest incurred for the years ended December 31, 1998, 1997 and 1996 was \$16,232,000, \$7,139,000 and \$6,327,000, respectively.

Minimum lease payments to be received under the terms of the operating lease agreements, excluding expense reimbursements, as of December 31, 1998, are as follows (in thousands):

1999	\$ 55,800
2000	50,759
2001	43,870
2002	38,459
2003	35,879
Thereafter	190,190
	\$ 414,957

Four

SECURED NOTE RECEIVABLE

In connection with the acquisition of a Life Science Facility in San Diego, California in March 1998, we made a \$6,000,000 loan to the sole tenant of the property, fully secured by a first deed of trust on certain improvements at the property. The loan bears interest at a rate of 11% per year, payable monthly, and matures in March 2002. The loan is cross-defaulted to the lease with the sole tenant. Under certain circumstances, we may obtain title to the improvements that secure the loan, and, in such event, we may also require the sole tenant at the property to lease such improvements back from us for an additional rental amount.

Five

UNSECURED LINE OF CREDIT

Alexandria has an unsecured line of credit which provides for borrowings of up to \$250 million. Prior to August 1998, our line of credit provided for borrowings of up to \$150 million. Borrowings under the line of credit bear interest at a floating rate based on our election of either a LIBOR based rate or the higher of the bank's reference rate and the Federal Funds rate plus 0.5%. For each LIBOR based advance, we must elect to fix the rate for a period of one, two, three or six months.

The line of credit contains financial covenants, including, among other things, maintenance of minimum market net worth, a total liabilities to gross asset value ratio, and a fixed charge coverage ratio. In addition, the terms of the line of credit restrict, among other things, certain investments, indebtedness, distributions and mergers. Borrowings under the line of credit are limited to an amount based on a pool of unencumbered assets. Accordingly, as we acquire additional unencumbered properties, borrowings available under the line of credit will increase, but may not exceed \$250 million. As of December 31, 1998, borrowings under the line of credit were limited to approximately \$214,000,000, and carried a weighted average interest rate of 6.48%.

The line of credit expires May 31, 2000 and provides for annual extensions (provided there is no default) for two additional one-year periods upon notice by the company and consent of the participating banks.

We enter into interest rate swap agreements to modify the interest characteristics of our outstanding debt. These agreements involve an exchange of fixed and floating interest payments without the exchange of the underlying principal amount (the "notional amount").

In September 1998, we entered into an interest rate swap agreement with BankBoston, N.A. (the "Bank") to hedge our exposure to variable interest rates associated with our line of credit. Interest paid is calculated at a fixed interest rate of 5.43% through May 31, 2000 on a notional amount of \$50 million and interest received is calculated at one month LIBOR. The net difference between the interest paid and the interest received is reflected as an adjustment to interest expense. The fair value of the swap agreement and changes in the fair value as a result of changes in market interest rates are not recognized in the financial statements. We are exposed to loss in the event the Bank is unable to perform under the swap agreement or in the event one month LIBOR is less than 5.43%.

In June 1998, the Financial Accounting Standards Board issued Statement No. 133, "Accounting for Derivative Instruments and Hedging Activities," which is required to be adopted in fiscal years beginning after June 15, 1999. When adopted, Statement 133 will require us to recognize all derivatives on the balance sheet at fair value. Based on the definitions provided in Statement 133, our interest rate swap agreement will be classified as a cash flow hedge, with changes in the fair value recorded as an adjustment to comprehensive income, which will be a separate component of shareholders' equity.

Six

SECURED NOTES PAYABLE

Secured notes payable consists of the following (in thousands):

	DECEMBER 31	
	1998	1997
9% note, due December 2014, secured by 3535/3565 General Atomics Court, San Diego, CA	\$ 17,578	\$ 18,050
7.75% note, due May 2016, secured by 1102/1124 Columbia Street, Seattle, WA	20,729	21,267
7.165% note, due January 2014, secured by 1431 Harbor Bay Parkway, Alameda, CA	8,500	8,500
8.68% note, due December 2006, secured by 100/800/801 Capitola Drive, Durham, NC	12,547	-
7.22% note, due May 2008, secured by 14225 Newbrook Avenue, Chantilly, VA and 3000/3018 Western Avenue, Seattle, WA	36,326	-
9.125% note due May 2007, with an effective interest rate of 7.25% (includes unamortized premium of \$2,262), secured by 620 Memorial Drive, Cambridge, MA	20,149	-
	<u>\$ 115,829</u>	<u>\$ 47,817</u>

All of our secured notes payable, except for the note secured by 1431 Harbor Bay Parkway, require monthly payments of principal and interest. The note secured by 1431 Harbor Bay Parkway required monthly payments of interest through December 31, 1998 and requires both monthly payments of interest and semi-annual principal payments beginning January 1999.

Future principal payments due on secured notes payable as of December 31, 1998, are as follows (in thousands):

1999	\$ 3,000
2000	2,907
2001	3,145
2002	3,395
2003	3,666
Thereafter	97,454
Subtotal	<u>113,567</u>
Unamortized premium	2,262
	<u>\$ 115,829</u>

Seven

ISSUANCE OF COMMON STOCK

On May 29, 1998, we sold 1,150,000 shares of our common stock to PaineWebber Incorporated for inclusion in the PaineWebber Equity Trust REIT Series I, a unit investment trust. The shares were issued at a price of \$30.5625 per share (before discounts and commissions) resulting in aggregate proceeds to us, net of offering costs of \$2.4 million, of approximately \$32.7 million.

Eight

NON-CASH TRANSACTIONS

During 1998, we assumed two secured notes payable in connection with the acquisition of the following properties (in thousands):

	100/800/801 Capitola Drive	620 Memorial Drive
Purchase price (including closing and transaction costs)	\$ 18,387	\$ 40,194
Cash paid for the properties	5,755	19,996
Secured notes payable assumed	\$ 12,632	\$ 20,198

Stock compensation expense in 1997 represents non-cash compensation expense associated with stock grants and stock options issued to our officers, directors and certain employees in connection with the Offering (see Note 11).

In connection with the Offering in 1997, all previously outstanding shares of Series U preferred stock and Series V preferred stock were converted into shares of common stock (see Note 1). The common stock issued was recorded at the book value of the Series U preferred stock and the Series V preferred stock (an aggregate of \$27,061,000).

Nine

PREFERRED STOCK AND EXCESS STOCK

Series V Cumulative Convertible Preferred Stock

Prior to the Offering, we had 27,500 shares of mandatorily redeemable Series V cumulative convertible preferred stock outstanding. The stated value of each share was \$1,000. In connection with the Offering, the shares were converted into 1,659,239 shares of common stock. The conversion rate was computed to provide for an internal rate of return on the stated value of each share equal to 20%, considering cash received from prior dividends.

Prior to conversion, Series V preferred stockholders were entitled to dividends at an annual rate of 10% of the stated value per share during the first twelve dividend periods or such larger amount as would be payable on an as converted basis if the Series V preferred stock were converted to common stock. Dividends were cumulative and payable in quarterly equal installments on March 31, June 30, September 30, and December 31 of each year. Offering costs associated with the issuance of the Series V preferred stock in 1996 were deducted from the proceeds of the issuance. Until the conversion of the Series V preferred stock into shares of common stock in 1997, we accreted the amount of the offering costs and the difference between the minimum yield requirement on the Series V preferred stock (20% per annum) and the minimum dividend payment as a charge to additional paid-in capital.

Series T and Series U Preferred Stock

Holders of each of the Series T and Series U preferred stock were entitled to dividends at an annual rate of 8.5% of the stated value per share. In connection with the Offering, all of the previously outstanding shares of Series T preferred stock (12 shares) were redeemed at their stated value (\$1,200 in the aggregate). In connection with the Offering, all of the previously outstanding shares of Series U preferred stock (220 shares) were converted into an aggregate of 7,354 shares of common stock.

Preferred Stock and Excess Stock Authorizations

Our charter authorizes the issuance of up to 100,000,000 shares of preferred stock and 200,000,000 shares of "excess stock" (as defined), none of which was issued and outstanding at December 31, 1998.

Ten

COMMITMENTS AND CONTINGENCIES

Litigation

We currently are not subject to any material legal proceedings or claims, nor are we aware of any material legal proceedings or claims being threatened.

Post-Retirement Benefit

In 1997, in connection with the Offering, an officer of Alexandria retired. In connection with the officer's retirement, we agreed to pay a post-retirement benefit equal to \$150,000 for each of the first three years following the Offering, and \$90,000 per year (plus an annual increase of 2% per year) thereafter for the remainder of the longer of the executive's life and the life of the executive's spouse as of the date of the agreement. In 1997 and 1996, a post-retirement expense was recorded for past services equal to \$632,000 and \$438,000, respectively (pursuant to a prior agreement). As of December 31, 1998 and 1997, the accrued liability for post-retirement benefit was \$1,110,000 and \$1,037,000, respectively. For the years ended December 31, 1998 and 1997, we paid \$150,000 and \$75,000, respectively, under the retirement agreement, of which \$77,000 and \$42,000, respectively, represented interest.

Employee Retirement Savings Plan

Effective January 1, 1997, we adopted a retirement savings plan pursuant to Section 401(k) of the Internal Revenue Code ("Code") whereby our employees may contribute a portion of their compensation to their respective retirement accounts, in an amount not to exceed the maximum allowed under the Code. The plan provides that we match the employees' contributions, which amounted to \$89,000 and \$36,000, respectively, for the years ended December 31, 1998 and 1997. Employees who participate in the plan are immediately vested in their contributions and in the matching contributions of the company.

Concentration of Credit Risk

We maintain our cash and cash equivalents at insured financial institutions. The combined account balances at each institution periodically exceed FDIC insurance coverage, and, as a result, there is a concentration of credit risk related to amounts in excess of FDIC insurance coverage. We believe that the risk is not significant.

We are dependent on rental income from relatively few tenants in the life science industry. The inability of any single tenant to make its lease payments could adversely affect our operations. As of December 31, 1998, we had 158 leases with a total of 148 tenants, and 24 of our 51 properties were leased to a single tenant. At December 31, 1998, our three largest tenants accounted for approximately 18.4% of our aggregate annualized base rent.

We generally do not require collateral or other security from our tenants, other than security deposits. As of December 31, 1998, we have \$6.1 million in irrevocable letters of credit available from certain tenants as security deposits for 15 leases.

Commitments

We are committed to complete the construction of a building and certain related improvements in San Diego, California at a remaining cost of approximately \$4.9 million under the terms of two leases. In addition, we are committed to complete the construction of a building and certain related improvements in Gaithersburg, Maryland at a remaining cost of between \$7.8 million and \$16.8 million (depending on the level of improvements to the facility elected by the tenant) under the terms of a lease. Under the terms of the lease, the tenant's rental rate will be adjusted depending on the ultimate cost of the improvements.

We are also committed to fund approximately \$11.1 million for investments in limited partnerships and rental properties, including the construction of tenant improvements under the terms of various leases. Of this amount, approximately \$3.2 million has been set aside in restricted cash accounts to complete the conversion of existing space into higher rent generic laboratory space (as well as certain related improvements) at 1102/1124 Columbia Street and 3000/3018 Western Avenue.

Eleven

STOCK OPTION PLANS AND STOCK GRANTS

We have elected to follow Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB 25") and related Interpretations in accounting for our employee and director stock options, stock grants and stock appreciation rights. Under APB 25, because the exercise price of employee and director stock options we granted equals the market price of the underlying stock on the date of grant, no compensation expense has been recognized.

1997 Stock Option Plan

In connection with the Offering, we adopted a stock option and incentive plan (the "1997 Stock Option Plan") for the purpose of attracting and retaining the best personnel, providing for additional incentives, and promoting the success of the company by providing employees the opportunity to acquire common stock. Options under our plan have been granted at prices that are equal to the market value of the stock on the date of grant and expire ten years after the date of grant. Employee options vest ratably in three annual installments from the date of grant. Non-employee director options are exercisable immediately upon the date of grant.

The options outstanding under the 1997 Stock Option Plan expire at various dates through November 2008. As of December 31, 1998, a total of 379,793 shares were reserved for the granting of future options under the 1997 Stock Option Plan.

Although we have elected to follow APB 25, pro forma information regarding net income and net income (loss) per share is required by Financial Accounting Standards Board Statement No. 123, "Accounting for Stock-Based Compensation." This information has been determined as if we had accounted for our employee stock options under the fair value method under Statement 123. The fair value of the options issued under the 1997 Stock Option Plan was estimated at the date of grant using a Black-Scholes option pricing model with the following weighted-average assumptions for 1998 and 1997:

	1998	1997
Risk-free interest rate	4.66%	5.82%
Dividend yield	5.2%	5.5%
Volatility factor of the expected market price	24.5%	28.7%
Weighted average expected life of the options	5 years	5 years

For purposes of the following pro forma disclosures, the estimated fair value of the options is amortized to expense over the options' vesting periods (in thousands, except per share information):

	FOR THE YEAR ENDED DECEMBER 31	
	1998	1997
Pro forma net income (loss)	\$ 18,299	\$ (3,096)
Pro forma net income (loss) per share:		
– Basic	\$ 1.51	\$ (0.38)
– Diluted	\$ 1.49	\$ (0.38)

A summary of the stock option activity under our 1997 Stock Option Plan, and related information for the years ended December 31, 1998 and December 31, 1997 follows:

	1998		1997	
	Stock Options	Weighted Average Exercise Price	Stock Options	Weighted Average Exercise Price
Outstanding-beginning of year	701,000	\$ 20.80	—	\$ —
Granted	290,500	31.00	701,000	20.80
Exercised	(57,333)	20.00	—	—
Forfeited	(112,667)	20.64	—	—
Outstanding-end of year	821,500	\$ 24.49	701,000	\$ 20.80
Exercisable at end of year	252,834	\$ 23.33	30,000	\$ 20.00
Weighted-average fair value of options granted		\$ 4.88		\$ 2.93

Exercise prices for options outstanding as of December 31, 1998 range from \$20.00 to \$32.94. The weighted average contractual life of options outstanding is 8.8 years.

Prior Stock Option Plan

Prior to the Offering, we had a ten-year incentive and nonqualified stock option plan for certain of our employees and non-employee directors.

Under this prior plan, holders of options to purchase common stock of Holdings granted under stock option plans of Holdings (“Holdings Stock Options”) were eligible, under certain circumstances (including the Offering), to receive substitute stock options of Alexandria in substitution for previously granted Holdings Stock Options. As such, in connection with the Offering, our officers, directors and certain employees received substitute stock options to purchase 57,000 shares of our common stock under the prior plan. These substitute stock options were exercised in connection with the Offering at a nominal exercise price. No further stock options were issued under the prior plan. In connection with the issuance of the substitute stock options, we recognized \$1,187,000 of stock compensation expense in 1997.

No compensation expense was recorded with respect to Holdings Stock Options issued during the year ended December 31, 1996 since they were issued with an exercise price equal to the then fair market value of the Holdings common stock.

Stock Grants

In connection with the Offering, we granted our officers, directors and certain employees an aggregate of 152,615 shares of common stock. As a result of the grants, we recorded stock compensation expense of \$3,052,000.

Twelve

PURCHASE OF ACQUISITION LLC

During January 1997, we assigned our right to purchase three Life Science Facilities to an entity (the “Acquisition LLC”) owned by affiliates of PaineWebber Incorporated (“PaineWebber”), the lead managing underwriter of the Offering. In January 1997, the Acquisition LLC acquired the three Life Science Facilities for \$51,871,000 from unaffiliated sellers. In connection with the Offering, we acquired 100% of the membership interests in the Acquisition LLC from the PaineWebber affiliates.

The purchase price we paid for the membership interests (\$58,844,000) exceeded the cost incurred by the Acquisition LLC to acquire the properties (\$51,871,000). The excess of this purchase price over the cost of the Acquisition LLC to acquire the properties (\$6,973,000) is reflected as a financing cost in 1997 in our consolidated statement of operations.

Thirteen

RELATED PARTY TRANSACTIONS

During 1998, 1997 and 1996, we incurred \$2,762,000, \$3,358,000 and \$1,708,000, respectively, for legal services provided by a firm of which a minority shareholder of Holdings is a member.

During 1998, 1997 and 1996, we were reimbursed \$270,000, \$21,000 and \$18,000, respectively, for payroll, accounting and office space incurred on behalf of Holdings.

Fourteen

QUARTERLY FINANCIAL DATA (UNAUDITED)

Following is a summary of consolidated financial information on a quarterly basis for 1998 and 1997:

	Quarter			
	First	Second	Third	Fourth
<i>(In thousands, except per share amounts)</i>				
1998				
Revenues	\$ 11,696	\$ 15,160	\$ 15,811	\$ 18,349
Net income	\$ 4,635	\$ 4,724	\$ 5,117	\$ 4,927
Net income per share:				
– Basic	\$ 0.41	\$ 0.40	\$ 0.41	\$ 0.39
– Diluted	\$ 0.40	\$ 0.39	\$ 0.40	\$ 0.39
1997				
Revenues	\$ 7,161	\$ 7,743	\$ 9,677	\$ 10,265
Net (loss) income	\$ (143)	\$ (10,989)	\$ 4,126	\$ 4,209
Net (loss) income per pro forma share (restated for the first and second quarters):				
– Basic	\$ (0.04)	\$ (1.80)	\$ 0.36	\$ 0.37
– Diluted	\$ (0.04)	\$ (1.80)	\$ 0.36	\$ 0.36

Fifteen

SUBSEQUENT EVENT

On February 23, 1999, we completed a follow-on offering of 1,150,000 shares of common stock (including the shares issued upon exercise of the underwriters' over-allotment option). The shares were issued at a price of \$28.125 per share resulting in aggregate proceeds, net of underwriters' discount and commissions, advisory fees and offering costs, of approximately \$29.6 million.

PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995

Certain statements made in this Annual Report constitute "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements involve known and unknown risks, uncertainties and other facts that may cause our actual results, performance or achievements, or industry results, to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Given these uncertainties, prospective and current investors are cautioned not to place undue reliance on such forward-looking statements. We disclaim any obligation to update any such factors or to publicly announce the result of any revisions to any of the forward-looking statements contained in this or any other document. Readers of this Annual Report should also read our other publicly filed documents for further discussion.

[REPORT OF INDEPENDENT AUDITORS]

ALEXANDRIA REAL ESTATE EQUITIES, INC.

To the Board of Directors and Stockholders of
Alexandria Real Estate Equities, Inc.

We have audited the accompanying consolidated balance sheets of Alexandria Real Estate Equities, Inc. and subsidiaries (the "Company") as of December 31, 1998, and 1997, and the related consolidated statements of operations, stockholders' equity, and cash flows for the years ended December 31, 1998, 1997 and 1996. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company as of December 31, 1998 and 1997, and the consolidated results of its operations and its cash flows for the years ended December 31, 1998, 1997 and 1996, in conformity with generally accepted accounting principles.

Ernst & Young LLP

Los Angeles, California
January 23, 1999, except for Note 15,
as to which the date is February 23, 1999

[DIRECTORS AND OFFICERS]

ALEXANDRIA REAL ESTATE EQUITIES, INC. AND SUBSIDIARIES

BOARD OF DIRECTORS

Jerry M. Sudarsky
Chairman of the Board of Directors
Alexandria Real Estate Equities, Inc.

Joel S. Marcus
Chief Executive Officer
Alexandria Real Estate Equities, Inc.

Joseph Elmaleh
Chemical Engineer and International Financier

Richard B. Jennings
President,
Realty Capital International, Inc.

Viren Mehta
President, Mehta Partners

David M. Petrone
Chairman of the Board,
Housing Capital Corporation

Anthony M. Solomon
Chairman, The Blackstone Alternate Asset
Management Advisory Board

Alan G. Walton
General Partner, Oxford Bioscience Partners

OFFICERS

Jerry M. Sudarsky
Chairman of the Board

Joel S. Marcus
Chief Executive Officer

James H. Richardson
President

Peter J. Nelson
Chief Financial Officer,
Senior Vice President –
Administration, Treasurer and Secretary

Lynn A. Shapiro
General Counsel

Steven A. Stone
Corporate Vice President

Vincent R. Ciruzzi
Vice President – Construction and Development

[CORPORATE INFORMATION]

ALEXANDRIA REAL ESTATE EQUITIES, INC. AND SUBSIDIARIES

COMMON STOCK

Listed on The New York Stock Exchange
Symbol ARE

CORPORATE OFFICE

135 North Los Robles Avenue
Suite 250
Pasadena, CA 91101
(626) 578-0777

TRANSFER AGENT

American Stock Transfer and Trust Company
40 Wall Street
New York, NY 10005
(212) 936-5100

LEGAL COUNSEL

Skadden, Arps, Slate, Meagher & Flom LLP
Los Angeles, California

AUDITORS

Ernst & Young LLP
Los Angeles, California

ANNUAL MEETING

The Annual Meeting of Shareholders will be held at 12:00pm, April 15, 1999 at the Hilton Hotel, Pasadena, California

SEC FORM 10-K

A copy of the Company's annual report to the Securities and Exchange Commission on Form 10-K is available without charge, upon written request to:

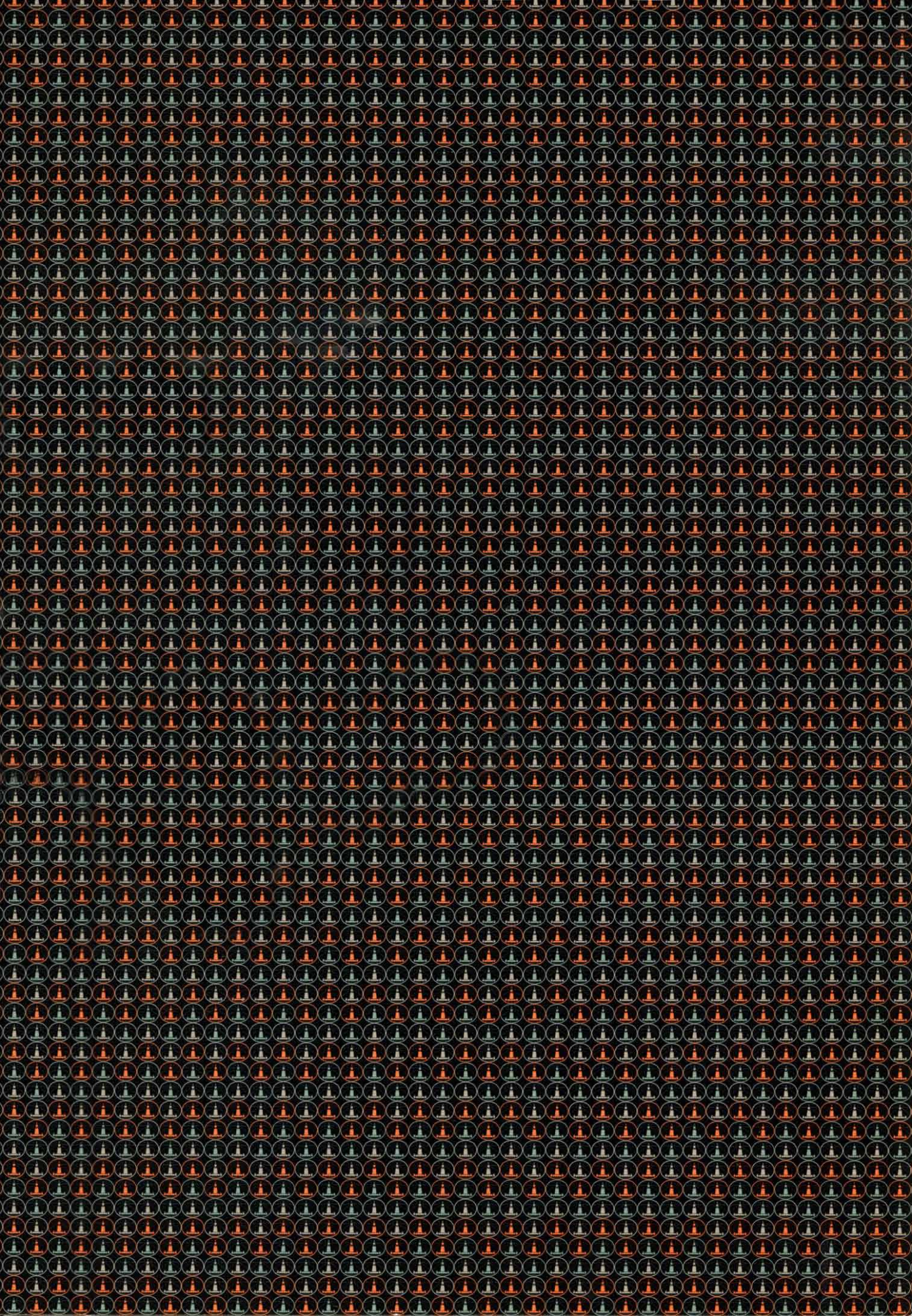
Investor Relations
Alexandria Real Estate Equities, Inc.
135 North Los Robles Avenue
Suite 250
Pasadena, CA 91101

COMMON STOCK DATA

The common stock of Alexandria Real Estate Equities, Inc. began trading on the New York Stock Exchange ("NYSE") on May 28, 1997 under the symbol "ARE." As of December 31, 1998, there were approximately 128 holders of record of the Company's common stock (excluding beneficial owners whose shares are held in the name of CEDE & Co.). The following table sets forth the quarterly high and low sales prices per share of common stock reported on the NYSE and the distributions paid by the Company for the year ended December 31, 1998.

PERIOD

PERIOD	High	Low	Per Share Distribution
January 1, 1998 to March 31, 1998	34 ⁹ / ₁₆	30 ⁷ / ₈	\$0.40
April 1, 1998 to June 30, 1998	34 ¹ / ₂	28 ¹ / ₂	\$0.40
July 1, 1998 to September 30, 1998	31 ¹¹ / ₁₆	25 ³ / ₁₆	\$0.40
October 1, 1998 to December 31, 1998	31 ¹⁵ / ₁₆	25 ¹⁵ / ₁₆	\$0.40





**COPYRIGHT ©1999 ALEXANDRIA REAL ESTATE EQUITIES, INC.
ALL RIGHTS RESERVED**